HEUBLEIN 1981 ANNUAL REPORT

SUPER-PREMIUM Smirnoff de Czar Vodka, pictured on the cover, was introduced just a year ago and is now available nationwide. This prestigious addition strengthens Heublein's position as the leading marketer of vodka, the nation's most popular type of distilled spirit. Smirnoff de Czar is among the many Heublein food and beverage products that are increasingly popular with consumers not only in the United States, but in markets all over the world. The photos in this year's annual report show an array of the brands whose quality and value helped Heublein achieve record results in a year of difficult economic conditions.

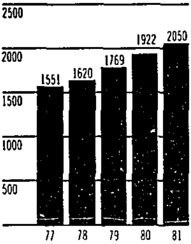
Contents

Heublein

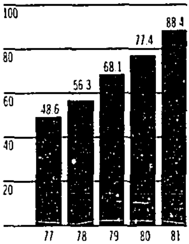
Financial Highlights

(In thousands except per share data)	1981	1980	% Increase
Revenues	**$2,050,121**	**$1,921,879**	**6.7%**
Income before income taxes	168,341	146,058	15.3
Income taxes	79,962	68,647	16.5
Net income	**88,379**	**77,411**	**14.2**
Dividends declared	38,036	34,566	10.0
Shareholders' equity	551,731	496,358	11.2
Average number of common shares outstanding	21,626	21,404	1.0
Per common share:			
Earnings — primary	$ 4.09	$ 3.62	13.0%
— fully diluted	3.93	3.48	12.9
Dividends declared	1.78	1.625	9.5
Shareholders' equity	25.59	23.20	10.3

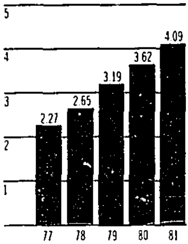
Revenues
(IN MILLIONS OF DOLLARS)



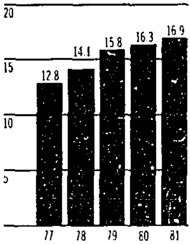
Income — Continuing Operations
(IN MILLIONS OF DOLLARS)



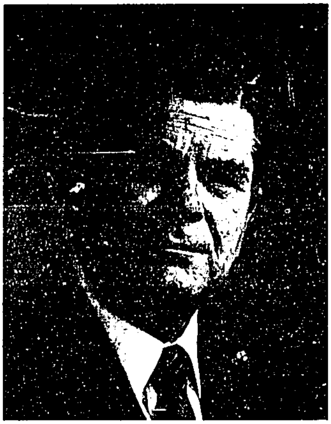
Earnings Per Share — Primary — Continuing Operations (IN DOLLARS)



Return On Shareholders' Equity — Continuing Operations (PERCENT)



Stuart D Watson



Hicks B Waldron

ATTAINING RECORD SALES and earnings in the food and beverage industries, in a year of constrained consumer buying, attests to Heublein's key strengths as a world marketer—the value of its products, product mix, brand leadership in growing markets, and the ability of its management, at all levels, to perform well under pressure.

These attributes and demonstrated flexibility in meeting challenging world conditions produced record overall results this year. At the same time, the company enhanced its human, technical and financial resources essential to future growth.

Net income was up 14 percent to more than $88 million, while revenues rose seven percent to top $2 billion for the first time.

While dealing with difficult market conditions here and overseas, respectable progress was made across a broad front of company activities.

- We registered a 31 percent gain in the operating profit of our worldwide food operations. Kentucky Fried Chicken clearly outperformed its competitors, and, along with the Grocery Products Group, boosted food revenues a solid 22 percent. Here in the United States, KFC company-owned stores set a new record of $427,000 in per-store average sales.
- We streamlined our organization into two worldwide operations—food and beverages—improving our mobility and flexibility to pursue opportunities. Each of these and the finance and administration operation, comprising all corporate staff functions, is headed by a senior vice-president reporting to the chief executive officer.
- KFC made record expenditures to expand and enhance the image of its stores overseas. They now total 1,256, up from 195 just ten years ago when we acquired KFC.
- Our alcoholic beverage revenues worldwide were down fractionally but operating profits were up. In total, it was a mixed performance, with spirits sales reflecting the general decline in spirits consumption that occurred in all major markets. Yet, Smirnoff Vodka's international sales were up six percent, just about as much as they were down in the U.S.
- Although the U.S. wine industry had a good year, United Vintners was off in sales and profits. However, with the Government's dismissal of the Federal Trade Commission's suit, which burdened us for a decade with the threat of having to dissolve Heublein's acquisition of U.V., the building of our wine business has begun in earnest.
- We drew closer to our goal of being a balanced food and beverage company as foods now account for 39 percent of corporate revenues and 41 percent of operating profit.

Because of its unique combination of strong product lines Heublein is a respected competitor in world markets and is seen as one with considerable potential.

Heublein is the world's number one producer of vodka, the most popular of all spirits; the world's number one retail chicken chain and the second largest U S. producer and marketer of spirits, of wines and of fast foods.

Last year 22 percent of corporate revenues and 25 percent of operating profit were derived from overseas operations

Where do Heublein's future opportunities lie?

Kentucky Fried Chicken can grow much more by applying its proven, business-building, "back-to-basics" program to the 3,679 franchisee stores in the U.S. and the 1,256 stores overseas.

Our Grocery Products Group has a rapidly growing market for its specialty foods, especially among the increasing number of young homemakers. Displaying considerable planning expertise, it capitalized on a growing consumer concern with food prices very early, emphasizing the value of its A.1 Steak Sauce, Grey Poupon Mustard and Mexican foods in its advertising. The results were record sales and earnings this year.

While worldwide spirits consumption slowed somewhat, the outlook remains quite positive. There were never more

consumers of drinking age than there are right now. Here in the U.S., the 25 to 44 year-age bracket will increase by some 15 million in the next ten years. Our marketing and advertising strategies are pointed directly at this opportunity because Heublein is well-positioned with leading brands in five of the fastest-growing spirits categories.

In wines the year's top news was that U.S. consumption, amounting to 478 million gallons, surpassed that of spirits for the first time. We expect that trend to continue as more and more consumers discover the delightful quality and value of California wines.

Sales of imported table wines in the United States were up 11 percent and our newly-formed International Vintage Wine Company shared in the increase, operating profitably in this its second year of operation.

A battle for market share is heating up among U.S. wine companies and competition through advertising and promotion is intensifying. Heublein is in a good position in this regard. It is one of the lowest cost producers of California wines having made its investments at a far more propitious time. It has excellent technical and production resources. It has an assured supply of high quality grapes and the widest range of wines of any company, from popular-priced brands, through standard table wines, to estate-bottled premiums.

Overseas, where our business, in recent years, has been growing at two to three times the rate of that in the U.S., we see opportunities abounding.

While the economies of other countries have suffered many of the same problems we have experienced, consumer lifestyle is beginning to change in many ways that should benefit our business. Consumer tastes have broadened. They are more venturesome concerning fast foods and mixed drinks. There's a growing preference for lightness.

For example, in major markets like the United Kingdom, Canada and South Africa, Smirnoff Vodka sales are moving steadily forward. They are rapidly approaching the six million case mark that it took nearly 40 years to reach in the U.S. and Smirnoff is just beginning to be discovered in many of these markets.

This year we broadened our distribution in Europe through joint ventures with the well-established firms of Cointreau and Cinzano.

In Brazil, where Heublein has the largest premium spirits and wines operation in that quarter of the globe, we are seeing the same emphasis on light drinks reflected in the increased consumption of vodka and wines. Our goal there is to increase our market share, keeping tight control of the balance sheet, despite a volatile economy with triple-digit inflation and interest rates, and to emerge in a strong competitive position when the economy improves.

KFC's business in Mexico, Japan and the United Kingdom was very good this year and in Australia it was excellent.

These are some of the highlights of operations that are described in detail on the following pages.

Our balance sheet improved markedly this year as we increased our cash and short-term investments by almost 100 percent, while incurring no additional long-term debt. We increased shareholders' equity and raised the dividend for the 21st consecutive year.

For sound business reasons, as well as a deep sense of social responsibility, we formed a top-level Minority Participation Council to set policy and guidelines for enhancing career opportunities in the Company and for increasing the use of minority-owned suppliers, agencies, and media. The Council is charged with monitoring and reporting the progress made by our operating groups under this policy.

In summary, Heublein has never been in a stronger position nor had more opportunities for growth The long-term demographics, economic and lifestyle trends definitely favor our businesses.

This year proved that we can meet the challenges of change by adapting, without departing from our basic, strategic plans. Five-year plans are in place and operating in every one of our major functions. Critical to these plans is the successful performance of our employees. This year proved that they are a team, with all the capabilities and motivation to get the job done and done well.

To put fiscal '81 in perspective, Heublein has emerged a stronger company with the resources, skills and vision needed to succeed in a worldwide economy We intend to invest our energies and resources in making a quantum thrust forward in the 80's

We are grateful for the support given by the Heublein team of loyal shareholders, dedicated employees and an active board of directors. We look forward to their continued support in fiscal '82. Our gratitude and best wishes are extended to Christopher W. Carriuolo, who is retiring as an officer and director after 22 years of valuable service.

We want to pay special tribute to an outstanding member of the Heublein team who passed away this year at age 90—Colonel Harland Sanders, founder of Kentucky Fried Chicken. His legacy of hard work, determination and unstinting devotion to quality will serve as a long-lasting inspiration to all of us at Heublein.

Stuart D Watson

Stuart D Watson
Chairman of the Board

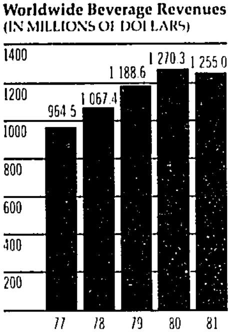
Hicks B Waldron

Hicks B Waldron
President & Chief Executive Officer

HEUBLEIN...WORLDWIDE OPERATIONS

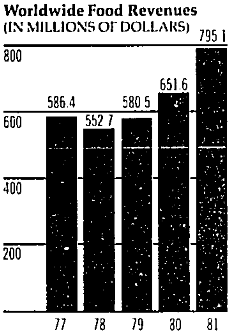
Heublein established a new operating structure this year to develop more effectively its food and beverage businesses in an expanding world economy. A concise overview of this new structure is given below.

BEVERAGE OPERATIONS



Heublein's worldwide beverage operations — consisting of the Spirits, Wines and International Beverages/Brazil Groups — accounted for 61 percent of corporate revenues and 59 percent of operating profit in fiscal 1981. Heublein holds a strong strategic position in the U.S. beverage market. It is second largest both in distilled spirits and in California wines, is a leader in imported wines, and has popular brands in the high growth segments of each category. Internationally, Heublein markets its brands in more than 100 countries and also operates the largest premium alcoholic beverage company in Brazil. John A. Powers is the Senior Vice President in charge of beverage operations.

FOOD OPERATIONS



Food operations in the United States and abroad accounted for 39 percent of corporate revenues and 41 percent of operating profit in fiscal 1981, with strong gains registered by all three groups: Food Service & Franchising, Grocery Products and International Foods. Reflecting the growing popularity of fast food, there now are more than 5,700 Kentucky Fried Chicken stores around the world, including 304 added this year. The Grocery Products Group's bellweather brand is A.1. Steak Sauce, which had record sales again this year. Michael A. Miles is the Senior Vice President in charge of food operations.

THE SPIRITS GROUP, based in Hartford, Conn., is Heublein's largest operating group in terms of revenues and operating income. It markets some of America's most popular beverage brands, including Smirnoff Vodka, Popov Vodka, Black Velvet Canadian Whisky, Heublein Cocktails, The Club Cocktails, Harveys Bristol Cream Sherry, Lancers Wine, Don Q Rum, Jose Cuervo Tequila and Arrow Cordials. Robert R. Weiss is the Group Executive.

THE WINES GROUP, with headquarters in San Francisco, produces the broadest range of popular wines of any U.S. vintner, from the premium Inglenook Vineyards brand to standard Colony Wines and the moderately priced Petri brand. The Group's principal wineries are in the Napa Valley, Asti, and Madera, Cal. John F. Keller is the Group Executive.

THE INTERNATIONAL BEVERAGES/BRAZIL GROUP, headquartered in Farmington, Conn., is responsible for marketing Heublein spirits and wines brands in more than 100 countries. Smirnoff is its chief product, but the Group also is making steady progress in introducing Heublein's prepared cocktails and California wines in new markets abroad. In Brazil, it markets a broad line of spirits, wines and aperitifs. Barry M. Rowles is the Group Executive.

THE FOOD SERVICE & FRANCHISING GROUP, based in Louisville, Ky., manages the Kentucky Fried Chicken system in the United States. The Group operates 775 company-owned KFC stores and works in partnership with franchisees who own and operate another 3,679 KFC stores. The Group also manages two other quick service restaurant operations: H. Salt Seafood and Zantigo America's Mexican Restaurants. Richard P. Mayer is the Group Executive.

THE GROCERY PRODUCTS GROUP, headquartered in Farmington, Conn., markets some of America's most popular brand name packaged foods, including A.1. Steak Sauce, Ortega Mexican foods and Grey Poupon Dijon Mustard. Its products are marketed through supermarkets, restaurants and cafeterias throughout the nation. Hugh R. Beath is the Group Executive.

THE INTERNATIONAL FOODS GROUP, in Louisville, Ky., is responsible for all Heublein's quick service restaurant operations outside the United States, including 1,256 Kentucky Fried Chicken stores in 50 countries. Consumer demand for Kentucky Fried Chicken continues to grow in most major markets. Michael A. Miles is the acting Group Executive.

BEVERAGE OPERATIONS

Heublein's worldwide beverage operations had mixed results this year. Overseas, sales increased again, aided by the increasing popularity of light, flavorful beverages such as Smirnoff Vodka. But U.S. sales declined slightly in the face of difficult economic conditions and a changing competitive environment.

Total beverage revenues for the year were $1,255,043,000, down one percent from $1,270,357,000 the prior year. Operating profit was up six percent to $133,629,000 from $125,996,000.

John A Powers
Senior Vice President
Beverage Operations

SPIRITS GROUP

While revenues for the Spirits Group declined one percent this year, operating profit held up well The Group continues to be the largest contributor to both corporate revenues and profits.

Revenues for the year were $812,410,000. Unit sales declined seven percent to 19.5 million cases

Operating Environment

An uncertain and sluggish economy and constrained consumer buying impeded industry growth for the second successive year. Total U.S. spirits industry sales were approximately 165 million cases, down somewhat from the previous year. Growth was recorded in several categories, however, including those in which Heublein has strong positions — vodka, Canadian whisky, tequila, rum and cordials

Non-whisky products continued to grow in popularity while traditional whiskies continued to decline, a trend that has prevailed for several years. As recently as 1970, non-whiskies accounted for only a third of all distilled spirits consumed in the U.S. Today they account for 51 percent of U.S. consumption and they are on the increase, a trend that favors Heublein.

As the battle among distillers for market share intensified during the year, many distillers became more competitive in their product advertising and promotion.

Factors in the spirits sales decline were high interest rates and cash flow problems that caused many wholesalers and retailers to reduce their inventories. On the positive side, however, economic pressures are prompting the trade to devote more promotion expenditures and shelf space to high volume, high profit brands such as those marketed by Heublein

Strategy for Growth

The Spirits Group's growth strategy includes.

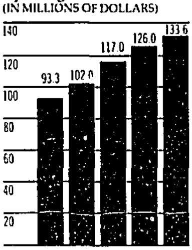
- Maintaining heavy advertising and promotion behind key premium brands.
- Developing innovative new products with high potential for long-term growth in sales and profits, and actively seeking candidates for joint business ventures and new brands to represent.
- Improving productivity through a combination of ongoing programs designed to reduce costs and increase operating efficiencies

Performance Highlights

The year's major developments at the Spirits Group included:

- An eight percent drop in shipments of Smirnoff Vodka, resulting from price increases taken early in the year that met with worse than expected market conditions. Corrective action was taken in two areas. Promotional pricing moves helped improve Smirnoff's sales picture in the second half of the year and a new marketing campaign, which emphasizes Smirnoff's

Worldwide Beverage Operating Profit
(IN MILLIONS OF DOLLARS)



Right Smirnoff Vodka is the perfect drink for a stylish tailgate party or for any festive occasion Because of its mixability, vodka is America's favorite distilled spirit — and premium quality Smirnoff is America's favorite vodka

Left Conferring at Corporate Headquarters are, left to right, Barry M. Rowles, Group Executive–International Beverages/Brazil Group, Robert R Weiss, Group Executive–Spirits Group, John F. Keller, Group Executive–Wines Group, and Charles J Herbert, President–Spirits Sales Division


SMIRNOFF
VODKA


HEUBLEIN

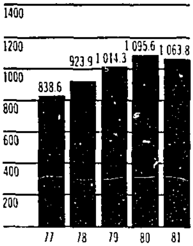
Left Convenience, quality and a wide variety of delicious flavors have made Heublein Cocktails and The Club Cocktails the nation's most popular brands of prepared drinks

Upper Right With sales approaching six million cases a year, Inglenook Vineyards wines are one of the nation's leading brands

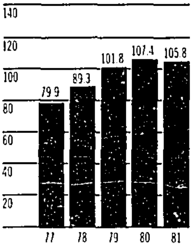
premiumness and value, was prepared for introduction early in fiscal 1982. With U.S. case sales of 6.4 million cases, Smirnoff is by far the nation's leading vodka and is among the strongest and most profitable of all spirits brands

- Smirnoff de Czar, the super-premium vodka introduced just a year ago, was moved into nationwide distribution This prestigious addition strengthens Heublein's position as the leading vodka marketer.
- Popov, with sales of over three million cases, continued its contribution as a strong entry in our vodka brand array.
- Arrow retained its position as the best-selling line of cordials in the U.S , introducing several new flavors, including the popular Honeydew Melon
- While the market for pre-mixed cocktails in general was negatively affected by the depressed U S economy, The Club Cocktails gained market share in the 200 milliliter size. Heublein Cocktails introduced two highly successful new flavors, Lime Daiquiri and Raspberry Daiquiri.
- José Cuervo Tequila, the leading brand in the growing tequila category, increased its sales to almost three-quarters of a million cases
- Black Velvet Canadian Whisky encountered consumer resistance after a price increase, and suffered a temporary setback in sales The brand regained momentum late in the year, however, sparked by a popular advertising and promotion program featuring TV actor Larry Hagman.
- Sales of Lancers Wines grew by seven percent, approaching the million case mark.
- Harveys Bristol Cream Sherry, supported by a series of effective TV commercials, made strong sales gains to exceed the half-million case level.
- Yukon Jack Canadian Liqueur, still a relatively new product with the potential for much broader distribution, grew faster than

Domestic Beverage Revenues
(IN MILLIONS OF DOLLARS)



Domestic Beverage Operating Profit
(IN MILLIONS OF DOLLARS)



any major Heublein brand and topped 200,000 cases for the first time

- Ten new products were introduced during the year including Jeremiah Weed, a 100° Bourbon-based liqueur, and several new flavors of cocktails and cordials. In addition, Viejo Vergel Brandy, the leading spirit brand in Mexico, and Rhum St James, a super-premium rum from the island of Martinique, were added to the Group's product portfolio.
- Heublein became the first multi-plant distiller authorized to operate its plants without the on-site presence of Federal Government inspectors Significant savings in time and money will result from the greater flexibility in transfer and storage of distilled spirits and reduced paperwork.

Despite this year's difficulties, the long-term outlook for the spirits industry is good The number of consumers in the prime consumer group of 25 to 44 year-olds will increase by some 15 million in the 1980s. The drinks projected to benefit most are those that are light, flavorful and go well with a wide range of mixers.

Left An informal evening of chamber music becomes even more enjoyable with the good taste and good value of Colony Classic wines, successfully introduced this year by the Wines Group

Upper Right These are among the more than 50 imported wines being marketed in the U S by Heublein's International Vintage Wine Company, which substantially increased its sales this year

Lower Right Beaulieu Vineyard's wines continued to win new honors this year Beaulieu Private Reserve Cabernet Sauvignon was named by Guide Gault-Millеau as one of the world's 12 finest wines It was the only U.S. wine to be chosen

The Spirits Group's plans for fiscal 1982 are targeted toward this broader market.

WINES GROUP

Revenues of the Wines Group declined 10 percent this year to $251,414,000, amidst heavier competition and changes in government regulations affecting the wine industry. At mid-year, following the dismissal of the Federal Trade Commission suit challenging Heublein's acquisition of United Vintners, the Group put its full energies behind new plans to compete more vigorously in the growing U.S. table wine market.

Operating Environment

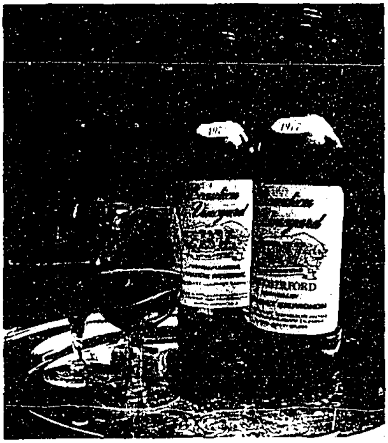
Wine continues to be the most rapidly growing segment of the alcoholic beverage business in the U.S. Industry sales were up approximately seven percent in 1981 to an estimated 478 million gallons. Most of the growth came in dry table wines, which now account for three of every four bottles of wine purchased.

California wines now hold an estimated 69 percent share of the U.S. wine market. In quality and value, they equal and often exceed the best of the imports

As more new wineries entered the market, competition increased and spending for advertising and promotion rose to record levels. Consumers, buffeted by high inflation and general economic uncertainties, were more price- and promotion-conscious than ever. This trend put added pressure on producers' profit margins.

Strategy for Growth

The Wines Group is concentrating its



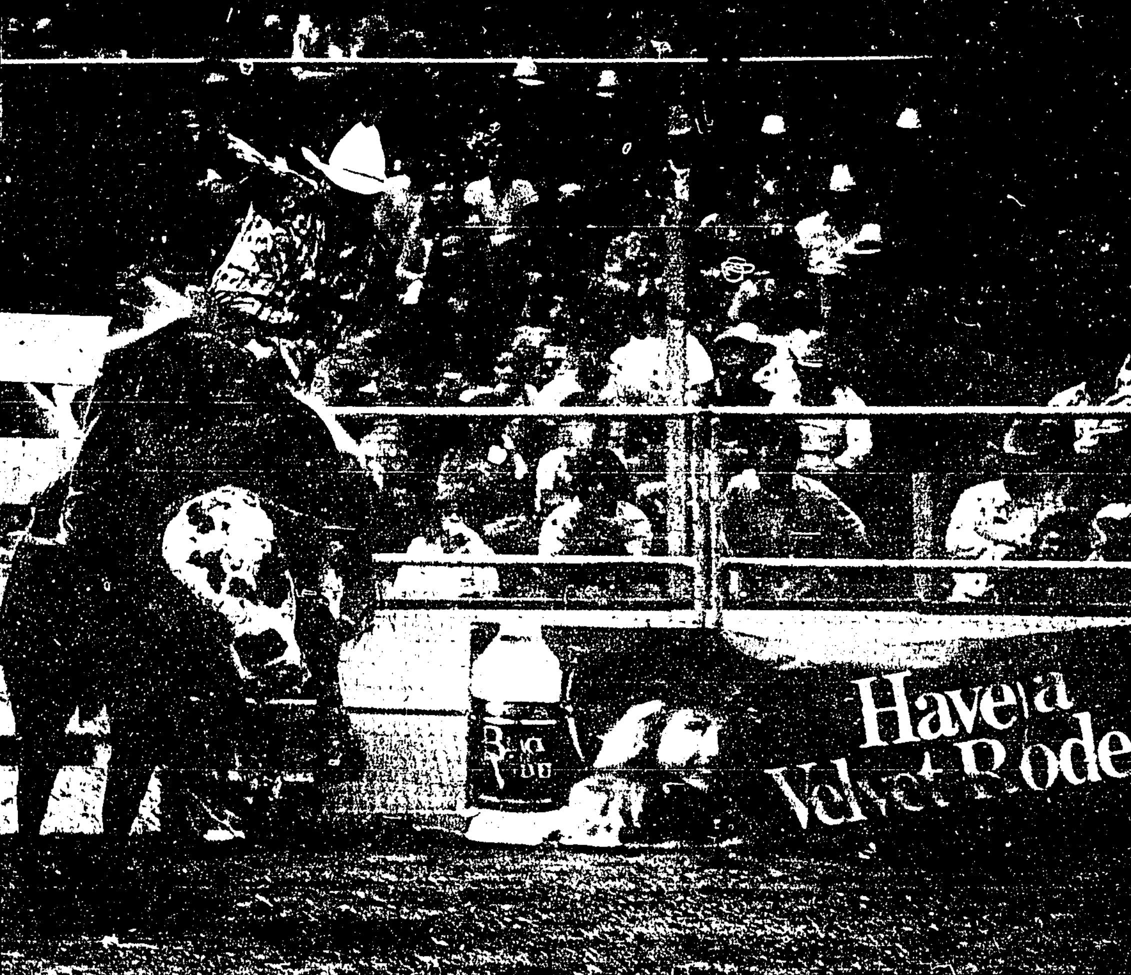
resources in the expanding, profitable dry table wine market. Its key strategies are:

- To support key brands with heavy investments in advertising and promotion, and to concentrate on superior execution of all sales programs at the wholesale and retail levels.
- To maintain the consistently high quality of its wines in all price categories.
- To achieve greater production and distribution efficiencies in order to provide maximum value to consumers.

Performance Highlights

Highlights of this year's performance by the Wines Group included:

- The successful introduction of four newly formulated Colony Classic wines and relabeling of the entire Colony line in a classical image. Introduction of the Colony Classics was backed by an extensive, hard-hitting advertising campaign which helped to generate excellent sales. The campaign spotlights results of a comparative consumer taste test in which Colony Classic Chablis was widely preferred over a more expensive competitive brand.
- The continued increase in sales of the premium Inglenook Vineyards brand to almost six million cases a year.
- The growth in sales of Petri Wines, reflecting the consumer search for good value in the lower-price range.


Have a


IMPORTE


SERRALLES
DON Q
GOLD

Left, above Sponsorship of action-packed professional rodeos throughout the nation helped promote sales of Black Velvet Canadian Whisky, which now approach two million cases a year

Left, below Black Velvet and Don Q Rum from Puerto Rico are two of the Spirits Group's popular imported brands

- Jacaré, the Group's line of premium proprietary wines, was introduced to five new markets and made strong sales gains Plans are in place for Jacaré's gradual expansion into full national distribution.
- Several of the Group's brands were repositioned to give them a stronger competitive edge, based on the findings of an intensive pricing study.
- Several key organization changes at the Wines Group provided a stronger, more experienced management team.
- The dismissal of the Federal Trade Commission lawsuit, after almost a decade of litigation, enabled the Wines Group to launch a forceful new growth plan

Heublein invested almost $100 million in the expansion and upgrading of its California wine facilities during the 1970s. In view of subsequent economic developments, this was a fortuitous investment, and as a result, the Wines Group can now produce quality wines in great quantity at relatively low cost. This is a real asset as the Group makes plans to return to a growth track.

BEAULIEU VINEYARD

Beaulieu Vineyard in Rutherford, California, is known to wine connoisseurs everywhere for its heritage of chateau-quality wines which rank with the finest anywhere in the world. In 1981, Beaulieu exceeded its profit goals, while investing in improved facilities to enhance further the quality of its wines.

Wines from Beaulieu were selected for President Reagan's first State Dinner at the White House, and for the White House dinner honoring England's Prince Charles. The prestigious international food and wine guide, Guide Gault-Milleau, selected Beaulieu Private Reserve Cabernet Sauvignon as one of the 12 finest wines in the world — the only American wine named to this elite list.

INTERNATIONAL VINTAGE WINE COMPANY

Established last year to spearhead the growth of Heublein's imported wine business, the International Vintage Wine Company (IVW) made significant progress this year. IVW expanded its selection of fine wines from around the world and increased its sales by 54 percent. The IVW product line includes more than 50 different wines from France, Hungary, Italy, Germany, Portugal and Japan.

Imported wine sales in the U.S. now exceed 100 million gallons a year and are growing rapidly. The International Vintage Wine Company is positioned to capitalize on that trend.

INTERNATIONAL BEVERAGES/BRAZIL GROUP

The combined International Beverages/ Brazil Group had another year of solid growth with gains in most major markets.

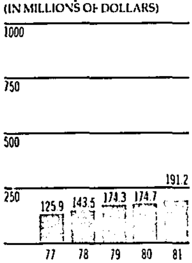
Revenues for the year increased nine percent to $191,219,000 from $174,808,000 a year earlier, accompanied by a strong increase in operating profit

Operating Environment

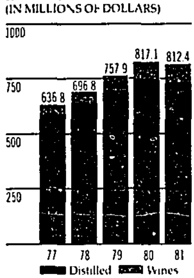
As many of the world's industrialized nations fought to combat inflation, the world economic environment was sluggish.

High inflation, high interest rates, rising unemployment and declining consumer disposable income characterized many major markets of the world In Brazil, where Heublein operates the largest premium spirits and wine company in that part of the world, an inflation rate of 120 percent and local interest rates that soared to 150 percent at the close of the fiscal year made business conditions difficult.

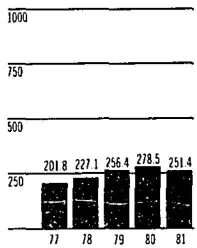
International Beverages/ Brazil Group Revenues
(IN MILLIONS OF DOLLARS)



Spirits Group Revenues
(IN MILLIONS OF DOLLARS)



Wines Group Revenues
(IN MILLIONS OF DOLLARS)




SMIRNOFF
VODKA

Left A mariachi band, good companions and a selection of flavorful Smirnoff drinks add *up to an exciting evening in* Mexico City. Smirnoff sales outside the U.S. increased to 5.8 million cases this year. It is the leading vodka in many major world markets.

Lower Right Conhaque Dreher and Smirnoff Vodka are among Heublein's many popular brands in Brazil, South America's largest alcoholic beverage market.

Under these economic pressures, alcoholic beverage sales grew at a much slower rate in many international markets. But vodka, and Smirnoff in particular, continued to grow because of the increasing consumer preference for lighter mixed drinks.

Strategy for Growth

In Brazil, Heublein's basic strategy is to focus on the non-whisky segments of the alcoholic beverage market, primarily vodka and selected wines, which are growing at double-digit rates. Emphasis also is being placed on strengthening Heublein's leading position in the premium-priced whisky category, which is relatively immune to economic slowdown. Another key element of Heublein's strategy in Brazil is to combat the volatile economic conditions with ongoing programs for cost reductions and even stronger balance sheet management and asset utilization.

In other overseas markets, Heublein has two key strategies.

First, to promote the growth of Smirnoff aggressively through strong marketing programs emphasizing the brand's heritage, its premium quality and its versatility.

Second, to broaden the overseas beverage business by launching other Heublein spirits and wine products in selected markets, emphasizing Heublein's pre-mixed drinks, which are ideally suited for the growing number of international consumers who prefer more flavorful drinks.

Performance Highlights

Highlights of the year's performance by the Group were.

- Smirnoff sales overseas grew six percent to 5.8 million cases. Gains were achieved in the largest foreign markets, including the United Kingdom, Canada, South Africa, Ireland and Sweden.
- Smirnoff was an exception to the decline in total spirits sales in the United Kingdom, where it increased its sales to more than 1.8 million cases and retained its 50 percent share of the growing vodka market.
- Total direct exports of Smirnoff from the U.S. exceeded 800,000 cases for the first time. Sales of 37,000 cases to Bulgaria gave Smirnoff its first major entry into the Eastern Bloc countries.
- At mid-year the Group entered into a series of joint ventures in Europe with the internationally-known French spirits company, Cointreau. Cointreau's strength in many European markets provides an effective base for developing Smirnoff and other Heublein brands in a large and economically strong area. Similarly, a joint venture in Spain with the Cinzano company will aid Smirnoff's development there.
- New Heublein wine and spirits products were launched in several key markets. Two of the most successful introductions were the Pina Colada in The Netherlands and Yukon Jack Liqueur in Canada. Smirnoff de Czar super-premium vodka was successfully tested in several countries, where it will soon be marketed. Heublein's premium Inglenook and Beaulieu wines were introduced in England, Ireland, Denmark and Belgium, and increased their sales in Canada, the Caribbean and other Western Hemisphere markets where they have been marketed for some time.
- While the alcoholic beverage industry in Brazil suffered a sales slowdown, Heublein gained market share. An aggressive profit improvement program in Brazil substantially reduced operating costs, helping to offset the impact of higher interest expense.
- A Business Development Department was formed by Heublein's Brazilian Company to search for new opportunities and develop profitable long-term growth strategies.

This year's results confirmed the great potential for Heublein in the vast and growing international spirits and wine markets.

Heublein's food operations in the United States and abroad posted excellent results in fiscal 1981. Total revenues increased 22 percent to $795,078,000 compared to $651,522,000 the prior year. Operating profit was up 31 percent to $90,671,000 from $69,206,000.

All three operating groups — Food Service and Franchising, International Foods and Grocery Products — contributed to this strong performance.

Michael A Miles
Senior Vice President
Food Operations

FOOD SERVICE AND FRANCHISING GROUP

The Kentucky Fried Chicken system in the U.S. continued to make solid progress in both the 775 company-owned stores and the 3,679 franchised stores.

Group revenues for the year totaled $385,750,000, up 19 percent from a year ago. Average annual sales at company KFC stores climbed 17 percent to $427,000 Real sales growth was up seven percent compared to five percent in 1980.

Operating Environment

The nation's quick service restaurant industry had a decline in customer traffic for the second consecutive year, feeling the effect of adverse economic conditions

Kentucky Fried Chicken company-owned stores again were an exception to the industry trend. They outperformed competition and strengthened KFC's position as the leader in the U.S. fast food chicken business. This accomplishment was all the more notable because of the increased competition from chicken chains and other chains that have added chicken to their menus.

Although poor economic conditions have curtailed the growth of the fast food industry these past two years, the following underlying trends favor the long-term growth of fast foods, particularly Kentucky Fried Chicken:

- Growth in the number of working women, single-member households, and 18–49 year-old consumers, all of whom are prime fast food customers.
- Increasing per capita consumption of chicken.
- The substantial and inherent price advantage of chicken over beef.
- Increasing emphasis on an active U S. lifestyle that favors the purchase of food away from home, with the emphasis on quality, convenience and value.

Strategy for Growth

Kentucky Fried Chicken's strategy for growth is to refine and extend the back-to-basics concept which has worked so well in the past four years. Franchisees are being encouraged to adopt these proven systems to improve their sales and profits

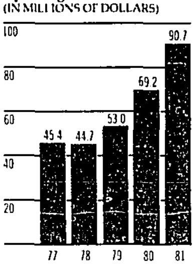
Special emphasis is being placed on quality, service and cleanliness; on capital investment in new stores and the remodeling of older units, and on programs to increase store sales, productivity and profitability

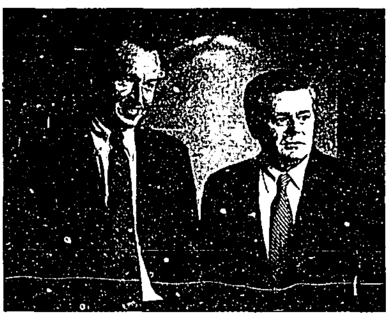
Performance Highlights

The most noteworthy achievements this year were:

- Dollar sales and volume increased each month over the previous year. At year's end, company-owned stores had achieved impressive real sales growth for 37 consecutive months.

Worldwide Food Operating Profit
(IN MILLIONS OF DOLLARS)





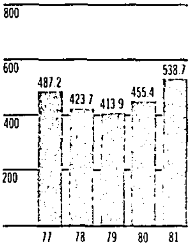
Right The Kentucky Fried Chicken system in the U S had record results this year, proving that consumers from coast to coast agree with KFC's new advertising slogan "We Do Chicken Right."

Left Hugh A Beath, left, is Group Executive–Grocery Products Group, and Richard P Mayer is Group Executive–Food Service and Franchising Group

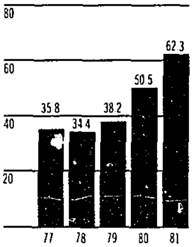
Left These classic car enthusiasts appreciate premium quality, and that's what they get with A 1 Steak Sauce, which transforms hamburgers into steakburgers Sales of A 1 were at a record level again this year, contributing substantially to the strong performance of the Grocery Products Group

- Average scores of 93 percent—the best ever—were achieved in store inspections for quality, service and cleanliness conducted periodically by mystery shoppers. This is a key indicator of customer satisfaction. Similar inspections conducted at competitive stores show that KFC's scores are consistently better, month to month, than all direct competition.
- Building on its successful advertising of recent years, KFC launched a new, aggressive national advertising campaign with the theme "We Do Chicken Right." It positions Kentucky Fried Chicken as the industry leader and the standard of excellence for fried chicken.
- Two new products were introduced: a real breast filet chicken sandwich and Kentucky Fries, natural cut fried potatoes Kentucky Fries are now available in all company stores and the chicken sandwich in most of them Both products began entering the franchise system this year and should be generally available in 1982.
- The company and its franchisees opened 94 new image stores and remodeled 199 existing stores as part of KFC's image enhancement program. To some degree, high interest rates slowed the building of new image stores by franchisees, but 597 stores meeting KFC's full new image standards were in operation at year's end. This is in addition to 467 that are company-owned and several hundred more units that are in the process of being converted to KFC's new image.
- During the year KFC Corporation acquired franchising rights for the state of Florida, formerly held by members of Col. Sanders' family. There are more than 175 franchised stores in Florida with sales of almost $50 million.
- Operating efficiencies of company stores continued to improve, thanks to a new inventory ordering and control system, a revised store staffing system, and more effective use of computerized electronic cash registers. The computerized registers permit hourly tracking of sales and the menu mix in each store, enabling field management to take prompt remedial action against potential problems
- Training programs were expanded and improved throughout the KFC system. The Corporate Training Center in Louisville conducted classes in store operations, business systems and technical operations for a record number of operating personnel Franchisee use of the STAR (Store Training and Rating) system for in-store training of hourly workers increased by 37 percent

Domestic Food Revenues
(IN MILLIONS OF DOLLARS)



Domestic Food Operating Profit
(IN MILLIONS OF DOLLARS)




Kentucky
Fried
Chicken

Left More than a thousand new image Kentucky Fried Chicken stores are now in operation throughout the U S Several hundred more units are in the process of being converted to the attractive new design, which has proven to be an effective method of helping increase customer traffic

The Kentucky Fried Chicken system in the U.S enters fiscal 1982 with the strong momentum generated by over three straight years of improved performance. The entire system is geared to capitalize on that momentum and to continue its growth in the new year

GROCERY PRODUCTS GROUP

The Grocery Products Group had outstanding results again this year, increasing its revenues 17 percent to a record $152,969,000 A.1. Steak Sauce and all of the Group's other major products achieved strong growth in sales to supermarkets, restaurants and other outlets

Operating Environment

In the past calendar year, the nation's $280 billion food industry continued to feel the effects of inflation. Dollar sales in the retail grocery sector grew about 11 percent, but tonnage, or real volume, was up only one and one half percent.

As prices increased, many consumers became more demanding, seeking products that offered the best value. To an increasing degree, consumers traded down from national brands to lower-priced private label and non-branded products

Added to this picture is the growth of warehouse food outlets, offering "no frills shopping" with limited brand choices Existing brands that are not leaders in their categories find it hard to achieve or maintain distribution in these outlets.

Strategy for Growth

In this demanding environment, the Grocery Products Group's strategy focused on developing and marketing specialty products that combine high quality, good value, and above-average profit margins.

The key strategy elements were

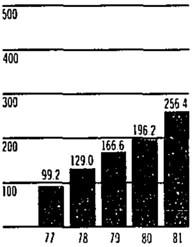
- Concentrating on the most "leverageable" aspect of each business unit, be it expanded usage by loyal customers or penetration of new, high potential market segments
- Investing a greater share of advertising and promotion funds in communications to consumers, strengthening their perception of the excellent value of the Group's products

Performance Highlights

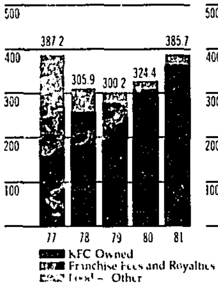
Highlighting the year's excellent performance by the Grocery Products Group were these developments·

- Sales of A.1. Steak Sauce set a new record despite the continued decline in the U S beef supply. Building on A 1 's reputation as the premium sauce for steak, the "Steakburger" national TV campaign helped establish A 1 as the sauce that adds value to less expensive cuts of beef—a powerful consumer message in a period of high beef prices. Sales also got a boost from a complementary campaign promoting the use of A.1. as a pour-in ingredient with ground beef.
- Grey Poupon, the only nationally distributed Dijon-style mustard in the U S , had its sixth consecutive year of double-digit growth. Key to this was a greater investment in consumer advertising.
- Sales of Regina Wine Vinegar, the leading product of its type, were increased by adding a new flavor, introducing new packaging and concentrating on greater distribution and shelf presence.

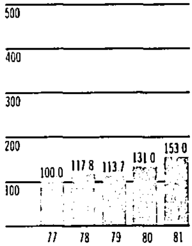
International Food Group Revenues
(IN MILLIONS OF DOLLARS)



Food Service and Franchising Group Revenues
(IN MILLIONS OF DOLLARS)



Grocery Products Group Revenues
(IN MILLIONS OF DOLLARS)

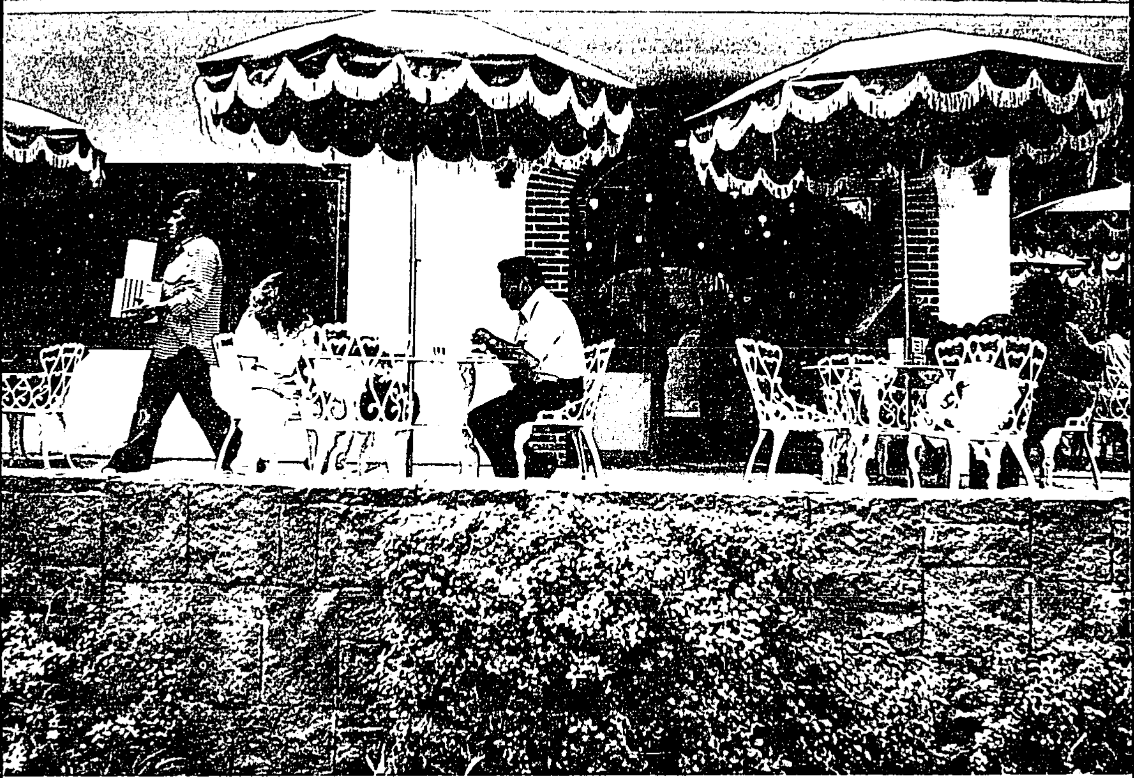


LA RECETA DEL CORONEL SANDERS

Kentucky Fried Chicken

DE MEXICO S.A. DE C.V.

como para chuparse los dedos



Left, above Outdoor tables are a popular feature of this Kentucky Fried Chicken store in Mexico, where KFC sales increased 30 percent this year

Left, below Kentucky Fried Chicken stores in Australia are being remodeled in the new image Per-store average sales for the 142 company-owned stores "Down Under" this year were $712,000, the highest for any company market in the world

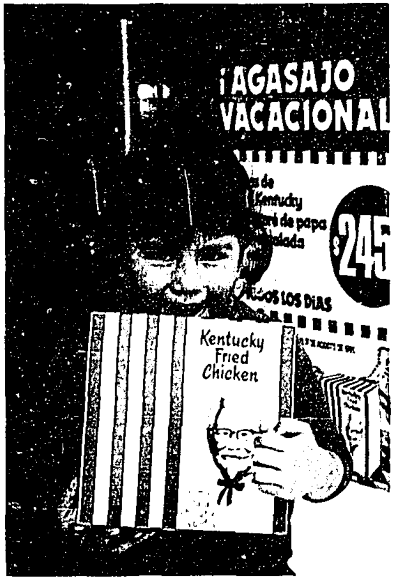
- Ortega Mexican products set a new volume record this year, reflecting the growing popularity of Mexican-type foods. Ortega Taco products and Ortega Chiles grew at double-digit rates. Attractive new packaging and carefully targeted advertising and promotion programs were major factors in Ortega's growth.
- Although the foodservice industry was generally flat for the year, the Group's Foodservice Operation achieved record increases in its sales of sauces and condiments and of Ortega products. It accomplished this with the help of a series of unique advertising and promotional programs that told operators of restaurants and cafeterias how to boost sales and profits by promoting expanded use of A.1. Steak Sauce, Grey Poupon Dijon mustard and Ortega Chiles and Salsas.
- Group management, concerned with inflation and high interest rates, continued to focus attention on balance sheet management. This resulted in reduced working capital requirements and an enhanced return on investment.
- Greater efficiencies were achieved in almost all areas of operation, particularly in manufacturing, warehousing and distribution.

Good planning and good execution have enabled the Grocery Products Group to grow rapidly in recent years despite the generally flat sales trends for the supermarket and foodservice industries. With its unique array of well-positioned, high growth brands, the Group anticipates another excellent year in fiscal 1982.

INTERNATIONAL FOODS GROUP

The International Foods Group, which is responsible for all Kentucky Fried Chicken operations outside the U.S., had excellent results this year. Revenues were up 31 percent to $256,359,000 compared to $196,140,000 a year ago

Revenues from KFC's overseas operations have tripled since 1975, and there are now 1,256 KFC stores doing business abroad in 50 countries, compared to 195 stores just 10 years ago when Heublein acquired KFC. There is great potential for continued rapid growth, both in existing markets and in others under development, such as Continental Europe and Latin America, where KFC's presence to date has been minimal.



Operating Environment

The business environment varied considerably this year in Kentucky Fried Chicken's major overseas markets. Looking at the economy in the three largest markets, Australia was booming, Japan was soft compared to its rapid growth of recent years, and the United Kingdom was weak. This was characteristic of the mixed economic conditions in other KFC markets around the world. But KFC's performance was generally good.

A common feature in most markets is the growing popularity of fast foods, led by Kentucky Fried Chicken, which operates more stores abroad than any other fast food chain.

Not unexpectedly, competition from quick service chicken and hamburger chains is increasing, although it is less intense than it is in the U.S. Kentucky Fried Chicken enjoys a significant competitive edge overseas by virtue of its established position and superior product.


Kentucky
Fried Chicken

Strategy for Growth

The growth strategy for Kentucky Fried Chicken overseas centers on expanding into new markets and increasing per-store sales by broader application of the programs that have proven so effective in achieving the highest standards of quality, service and cleanliness

The strategy also calls for building additional stores in key markets, upgrading existing stores and implementing systems to increase the efficiency of store operations. Additionally, the Group's organization worldwide is being strengthened and there is more emphasis on in-depth marketing research.

Performance Highlights

Highlights of the year's performance by the International Foods Group include.

- More than 125 new stores were opened and per-store average sales made substantial real gains in most markets.
- In Australia, per-store average sales for the 142 company-owned stores increased 19 percent to $712,000, the highest for any company market in the world.
- Another 49 stores were opened in Japan, bringing the total in this fast-growing market to 324. Per-store sales in company stores increased 13 percent. Continued rapid expansion is planned in Japan, which has a population about half that of the U.S., but only about seven percent as many KFC stores.
- Despite depressed economic conditions in the United Kingdom, KFC sales continued their steady increase in the 322 KFC stores there. Starting from a low base of $89,000 in 1975, average sales at company-owned stores have increased to $366,000 this year, a compound annual growth rate of 27 percent.
- KFC sales in Mexico increased 30 percent this year and have almost doubled since 1979. This is another potential high growth market for KFC. At present there are just 54 KFC stores in Mexico, and the country is experiencing the fastest economic growth of any KFC market.

Left Japan is one of the largest overseas markets for Kentucky Fried Chicken with 324 stores in operation Continued rapid expansion is planned for the KFC system in Japan

- Mystery shopper programs that provide for the inspection of KFC stores for quality, service and cleanliness were expanded and improved in most KFC markets overseas, helping to increase customer traffic and sales

Economic conditions in all key Kentucky Fried Chicken markets in the coming year are expected to be as good as or better than they were in fiscal 1981 and the outlook is for political stability in all these areas These favorable conditions should enable Kentucky Fried Chicken to continue its solid growth overseas.

REVIEW OF FINANCE AND ADMINISTRATION

Corporate Finance and Administration is the third major unit in Heublein's new organizational structure, complementing Beverage Operations and Food Operations. It comprises five corporate staff departments, all reporting to Gwain H. Gillespie, Senior Vice President for Finance and Administration.

Gwain H Gillespie
Senior Vice President
Finance and
Administration

Company Strengthens Its Financial Position

The economic environment presented many challenges throughout the year — double digit inflation in the United States and most foreign countries, record high interest rates for Heublein and for our customers, and significant changes in foreign currency exchange rates.

The Company responded by placing renewed emphasis on cash management, improving inventory and receivable turnover and rigorous scrutiny of our capital expenditures These efforts were fruitful, as reflected in several key measurements of Heublein's financial strength.

While sales were up $128 million, or 7%, the company's investment in receivables and inventories to support these sales increased only $7 million, or 1%. This performance was aided by new and improved asset management programs at the operating groups and at the corporate level

The company's cash and temporary investments at June 30, 1981, increased by $37 million over the prior year to a record $75 million. More than 90% of this was invested in interest-bearing instruments, and there were no short-term domestic bank borrowings at year's end

The majority of the company's working capital requirements was provided by funds from operations, principally net income plus depreciation These sources provided $131 million in 1981, exceeding the $102 million required by capital expenditures and dividend payments The 1981 dividend payout marked the 21st consecutive year of increased payments to Heublein's shareholders.

The company's year-end ratio of debt to debt-plus-shareholders' equity was 30%, the best in more than a decade. Fixed interest debt comprising nearly 80% of total debt carried an average interest rate of 6.3%. The relatively low ratio of total debt to total capitalization, together with available funds from a revolving credit agreement, puts the company in a good position to consider acquisitions.

Return on shareholders' equity, another measure of the company's ability to manage its financial resources, improved again. This has grown in each of the past five years, from 12 8% in 1977 to 16.9% in fiscal 1981.

Advertising, merchandising and sales promotion expenditures were a record $187 million in fiscal 1981. These expenditures represent one of Heublein's most important investments in the growth of its business.

Additional financial highlights are shown in the financial statements and graphs that appear throughout this report.

Major Litigation Resolved

In the legal area, final resolution was achieved in the Federal Trade Commission suit and the shareholder suit pertaining to the company's Loan Guaranty and Stock Option Programs With these matters behind us, the company is no longer burdened with these time-consuming distractions to its management.

The highly effective legal education program for all management employees was strengthened this year. In keeping with management's commitment to compliance with all laws and regulations pertaining to Heublein's business in the U.S. and abroad, this pro-active program is designed to prevent violations that might occur due to unfamiliarity with the many laws and regulations and their application to company activities.

Human Resources Programs Upgraded

In the human resources area, there was a broad upgrading of several key programs that assist Heublein in hiring, retaining and motivating top quality personnel

All exempt positions in the company were re-evaluated and graded in order to assure internal parity and external competitiveness. A new performance appraisal system was installed, giving

At left are the corporate vice presidents in charge of Heublein's corporate staff departments From left to right are George Caspar, Secretary and General Counsel, Robert W Pratt, Jr, Planning and Research, Joseph M McGarry, Communication and Public Affairs, William W Mauritz, Human Resources, Gene R Ehnen, Finance and Controller, and John J Moran, Assistant to the Chairman

managers an effective tool for improving individual job performance throughout the company.

Several benefits programs were improved and expanded, including Heublein's Employee Assistance Program, which has helped more than 1,000 employees deal with personal and family problems in its five years of operation

Social Responsibility Programs Expand

The Minority Participation Council, formed this year, made encouraging progress in achieving greater participation by minorities in a broad range of business activities throughout the company Affirmative action is now part of the annual performance review of every Heublein executive with responsibility for hiring and, this year, 40 minority employees and 33 women advanced into professional and management positions in our company

As an important part of the company's social responsibility program, The Heublein Foundation again increased its financial support to programs benefiting education, health, welfare, culture and art. Several organizations that are combating alcohol abuse continued to receive substantial assistance.

Efforts in the Public Affairs area were instrumental in achieving favorable tax treatment for our wine and spirits products These rulings helped counter the negative impact of the 1980 Multinational Trade Agreement, which unduly favored competitors who are major importers of distilled spirits.

Heublein's Premiere National Auction of Rare Wines, conceived as a public service vehicle for fostering appreciation of U.S. wines, continued to be a highly effective vehicle for promoting California wines

More Emphasis Placed on Planning and Research

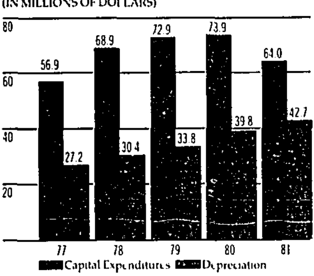
New emphasis was given to the planning and research functions this year, reflecting their increasing importance in successfully competing in a rapidly changing worldwide environment.

Marketing Research completed more than 300 studies during the year, providing extensive information to assist in developing new advertising and marketing strategies for Smirnoff, Kentucky Fried Chicken and other key brands in the U S. and abroad

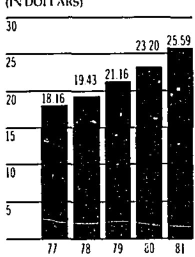
With planning disciplines successfully established in the operating groups, Strategic Planning concentrated on assisting management in the development of long-term corporate objectives and strategies.

Economic and Environmental Research provided management with assessments of potential threats and opportunities posed by developments in such areas as the economy, social change, lifestyles, and government legislation and regulation.

Capital Expenditures/Depreciation
(IN MILLIONS OF DOLLARS)



Shareholders' Equity—Per Share
(IN DOLLARS)



Principles of Consolidation	The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries The Company's investments in affiliated companies (not majority-owned) are accounted for on the equity basis, and the Company's operating results include its share of their net income. All significant intercompany transactions are eliminated in consolidation
Inventories	Inventories are stated at lower of cost or market Cost is determined by specific lots, the first-in, first-out (FIFO) method and, beginning in 1980, the last-in, first-out (LIFO) method for certain domestic inventories (see Inventories note) Bulk whiskey and wine in storage for aging over a number of years are included in current assets in accordance with industry practice.
Property, Plant and Equipment	Property, plant and equipment are carried at cost Depreciation and amortization are computed generally by the straight-line method over the estimated useful lives of the respective assets or the terms of the related leases. On sale or retirement, the asset cost and related accumulated depreciation are removed from the accounts, and any related gain or loss is reflected in income.
Cost in Excess of Net Assets of Purchased Businesses, Trademarks, Contracts and Franchises	Cost in excess of net assets of purchased businesses is being amortized on a straight-line basis over periods ranging from 5 to 40 years, except for $4,016,000 relating to an acquisition prior to November 1, 1970 which is not being amortized as, in the opinion of management, there has been no diminution in value. Trademarks, contracts and franchises are carried at cost less amortization which is being provided on a straight-line basis over periods ranging principally from 5 to 40 years.
Franchise and License Fees	Initial franchise fees are recorded as income on the date the store is opened by the franchisee Monthly fees from franchisees and licensees are accrued as earned
Taxes	Deferred income taxes result from timing differences between tax and financial recognition of income and expense. The principal items causing timing differences are provisions for losses on disposition of discontinued operations and accelerated depreciation. The investment tax credit is deducted from federal income tax expense in the year in which the related asset is placed in service. United States and Canadian excise taxes constitute a lien on in-bond inventories. Since these taxes are not payable until withdrawal from bond, excise taxes have not been accrued with respect to such inventories in accordance with industry practice.
Pension Plans	The Company has non-contributory retirement plans which cover substantially all full-time domestic employees except certain employees covered by union pension plans. Under collective bargaining agreements, the Company makes contributions to various pension plans for certain union employees Pension costs charged to current earnings include charges for current service and amortization of prior service costs over 30 years The Company's policy is to fund amounts accrued.
Earnings Per Share	Primary earnings per share are based on the weighted average number of common and common equivalent shares outstanding during each year. Fully diluted earnings per share also include the effects of the remaining dilutive stock options and convertible securities.

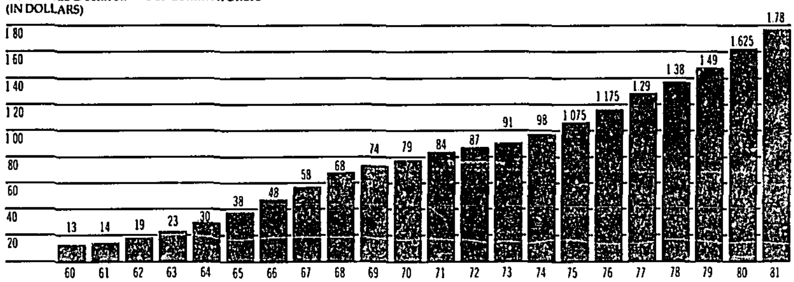
Heublein

Consolidated Statement of Income

(In thousands except per share data)	Year ended June 30, 1981	1980	1979
Revenues:			
Net sales	$1,984,396	$1,865,474	$1,719,222
Franchise and license fees	65,725	56,405	49,852
	2,050,121	**1,921,879**	**1,769,074**
Costs and expenses:			
Cost of sales	1,381,606	1,325,293	1,222,693
Selling, advertising, administrative and general expenses	444,215	401,384	376,405
	1,825,821	1,726,677	1,599,098
Operating profit	224,300	195,202	169,976
Other deductions:			
Interest expense:			
Long-term debt	12,636	14,315	13,077
Other	15,945	11,046	10,029
Corporate and miscellaneous — net	27,378	23,783	15,851
	55,959	49,144	38,957
Income before income taxes	168,341	146,058	131,019
Income taxes	79,962	68,647	62,889
Net income	**$ 88,379**	**$ 77,411**	**$ 68,130**
Earnings per share:			
Primary	**$4.09**	**$3.62**	**$3.19**
Fully diluted	**$3.93**	**$3.48**	**$3.09**

See accompanying notes and summary of accounting policies

Dividends Declared — Per Common Share
(IN DOLLARS)



Consolidated Balance Sheet

(In thousands)	June 30, 1981	June 30, 1980
ASSETS		
Current assets:		
Cash and temporary investments	$ 74,761	$ 37,884
Accounts and notes receivable	199,497	195,780
Inventories		
Finished products	97,646	101,158
Products in process	7,157	8,237
Bulk whiskey and wine	165,433	156,964
Raw materials	34,133	34,312
Total inventories	304,369	300,671
Deferred income tax benefits	19,015	20,834
Prepaid expenses	11,947	9,378
Total current assets	**609,589**	**564,547**
Investments in and advances to affiliated companies	**20,978**	**19,826**
Property, plant and equipment – net	**388,594**	**372,043**
Other assets:		
Cost in excess of net assets of purchased businesses	53,070	53,833
Trademarks, contracts and franchises	13,645	2,675
Other	35,063	34,095
	101,778	**90,603**
	$1,120,939	**$1,047,019**

Heublein

	June 30,	
	1981	1980
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Notes payable	$ 34,204	$ 28,177
Current portion of long-term debt	4,305	5,572
Current obligations under capital leases	2,616	2,900
Accounts payable	77,491	80,061
Accrued expenses	90,181	81,898
Taxes		
Federal, state and foreign income taxes	44,942	28,189
Excise taxes	50,877	54,846
Other taxes	8,628	9,019
Dividends payable	9,794	8,886
Total current liabilities	**323,038**	**299,548**
Long-term debt due after one year	**199,649**	**201,306**
Capital lease obligations	**24,262**	**24,132**
Other long-term liabilities	**15,536**	**20,328**
Minority interest in foreign subsidiaries	**6,723**	**5,347**
Shareholders' equity:		
Preferred stock:		
Series A	866	927
Series B	220	244
Common stock	10,760	10,673
Additional paid-in capital	152,606	147,578
Retained earnings	387,279	336,936
Total shareholders' equity	**551,731**	**496,358**
	$1,120,939	**$1,047,019**

See accompanying notes and summary of accounting policies

Consolidated Statement of Additional Paid-in Capital

(In thousands)	Year ended June 30, 1981	1980	1979
Balance at beginning of year	**$147,578**	**$144,739**	**$144,204**
Excess of option price over stated value of common stock issued on exercise of options	3,089	1,268	487
Excess of fair market value over stated value of restricted stock issued	1,511	1,476	—
Excess of stated value of preferred stock converted over stated value of common stock issued	3	3	4
Tax benefit from exercise of options issued under stock option plans	425	92	44
Balance at end of year	**$152,606**	**$147,578**	**$144,739**

Consolidated Statement of Retained Earnings

(In thousands except per share data)	Year ended June 30, 1981	1980	1979
Balance at beginning of year	**$336,936**	**$294,417**	**$257,918**
Net income	88,379	77,411	68,130
Dividends declared on common stock — $1 78 per share ($1.625 in 1980 and $1.49 in 1979)	(38,036)	(34,566)	(31,631)
Cancellation of treasury shares	—	(326)	—
Balance at end of year	**$387,279**	**$336,936**	**$294,417**

See accompanying notes and summary of accounting policies

Dividends Paid & Stock Price Ranges

	Quarter	Dividends Paid	Stock Price Range* High	Low
1981	4	$ 455	$35¼	$29¾
	3	455	34	27½
	2	415	30½	24¾
	1	415	34½	29⅝
1980	4	$ 415	$31¼	$24⅝
	3	415	32¼	23⅝
	2	38	32⅝	26¾
	1	38	30¼	25⅝

*New York Stock Exchange (symbol HBL)
Holders of record at July 31, 1981 — 22,322.

Consolidated Statement of Changes in Financial Position

(In thousands)	Year ended June 30, 1981	1980	1979
SOURCES OF WORKING CAPITAL			
Operations			
Net income	$ 88,379	$ 77,411	$ 68,130
Charges (credits) not requiring funds:			
Depreciation and amortization	42,722	39,806	33,837
Deferred income taxes	2,857	1,608	(1,186)
Equity in unremitted earnings of unconsolidated affiliates	(4,428)	(3,559)	(4,033)
Minority interest in earnings of foreign subsidiaries	1,376	228	821
Funds provided from operations	130,906	115,494	97,569
Book value of assets sold	8,036	10,402	11,164
Increase in long-term debt	5,791	5,426	13,032
Increase in investments in and advances to affiliated companies	3,013	3,751	2,250
Increase in common stock and additional paid-in capital resulting from exercise of stock options and issuance of restricted stock	5,112	2,889	541
Other — net	104	154	1,027
	152,962	138,116	125,583
USES OF WORKING CAPITAL			
Additions to property, plant and equipment	63,984	73,854	72,896
Dividends declared	38,036	34,566	31,631
Additions to cost in excess of net assets of purchased businesses, trademarks, contracts and franchises	12,889	357	7,674
Reduction of long-term debt	7,448	12,496	3,353
Increase in other assets	1,534	8,384	538
Decrease (increase) in other long-term liabilities	7,519	520	(2,812)
	131,410	130,177	113,280
Increase in working capital	**$ 21,552**	**$ 7,939**	**$ 12,303**
CHANGES IN WORKING CAPITAL			
Cash and temporary investments	$ 36,877	$ (14,958)	$ (12,653)
Accounts and notes receivable	3,717	15,387	9,475
Inventories	3,698	25,819	57,155
Deferred income tax benefits	(1,819)	10,390	4,050
Prepaid expenses	2,569	2,580	(2,468)
Notes payable, current portion of long-term debt and current obligations under capital leases	(4,476)	(12,553)	5,390
Accounts payable, accrued expenses and taxes	(18,106)	(17,970)	(47,989)
Dividends payable	(908)	(756)	(657)
Increase in working capital	**$ 21,552**	**$ 7,939**	**$ 12,303**

See accompanying notes and summary of accounting policies

Taxes

The components of income tax expense for fiscal 1981, 1980 and 1979 follow:

	1981	1980	1979
		(In thousands)	
Current:			
Federal	$ 54,177	$ 50,982	$ 50,354
State	11,391	9,078	9,211
Foreign	11,537	6,979	4,510
	77,105	67,039	64,075
Deferred			
Federal	2,450	1,985	(386)
Foreign	407	(377)	(800)
	2,857	1,608	(1,186)
Total income tax expense	$ 79,962	$ 68,647	$ 62,889

The provision for federal income taxes includes deferred tax charges (credits) resulting from the following:

	1981	1980	1979
		(In thousands)	
Excess of tax over book depreciation	$ 1,835	$ 2,077	$ 1,670
Losses from discontinued operations provided for in prior periods	2,104	791	556
Other items	(1,082)	(1,260)	(3,412)
Provision (benefit) for deferred income taxes	$ 2,857	$ 1,608	$ (1,186)

The components of income before income taxes follow.

	1981	1980	1979
		(In thousands)	
United States	$146,222	$130,066	$121,057
Foreign	22,119	15,992	9,962
Total	$168,341	$146,058	$131,019

The consolidated effective income tax rate was 47.5% for 1981, 47% for 1980 and 48% for 1979 Significant items affecting these rates were 3 7% in 1981, 3.4% in 1980 and 3.7% in 1979 due to state and local taxes, net of federal income tax benefit; and (1.1)%, (2 2)% and (3.1)%, respectively, due to investment tax credits

No provision for federal income taxes has been made for the undistributed earnings of foreign subsidiaries since it is management's intent to reinvest substantially all earnings of foreign subsidiaries abroad. If such earnings were distributed, income tax credits would be available to substantially reduce any resulting income tax liability

Net sales include excise taxes of $458,713,000 in 1981, $491,829,000 in 1980 and $465,682,000 in 1979

Inventories

Effective July 1, 1979, the Company adopted the LIFO method of valuing certain inventories in its domestic beverage and food operations The change from specific lot and FIFO methods for these inventories was made to match more closely current costs with current revenues The effect of this change was to reduce net income by $4,713,000 or $.22 per share for fiscal 1981 and $4,124,000 or $ 19 per share for fiscal 1980 It is not practical to restate earlier years or to determine the cumulative effect of the change to LIFO.

Had these inventories been valued using the specific lot and FIFO methods rather than the LIFO method, inventories would have been $16,759,000 and $7,781,000 higher than those stated at June 30, 1981 and 1980, respectively

Property, Plant and Equipment

Property, plant and equipment are summarized by major classification as follows

	June 30, 1981	June 30, 1980
	(In thousands)	
Land and land improvements	$ 64,176	$ 57,103
Buildings	128,079	120,901
Machinery and equipment	261,542	247,786
Leasehold improvements	87,341	76,256
Capital leases (principally buildings)	35,552	35,196
Construction in progress	25,056	20,934
	601,746	558,176
Less accumulated depreciation and amortization	213,152	186,133
	$388,594	$372,043

Accumulated amortization pertaining to capital leases, included above, amounted to $13,524,000 and $13,392,000 at June 30, 1981 and 1980, respectively.

Temporary Investments and Short-Term Borrowings

Temporary investments, consisting principally of commercial paper and U.S. Government obligations, amounted to $68,475,000 and $19,510,000 at June 30, 1981 and 1980, respectively

At June 30, 1981 and 1980, the Company had available unsecured lines of credit from several domestic banks aggregating $53,000,000 and $51,880,000, respectively, and from foreign banks aggregating $38,763,000 and $54,902,000, respectively

The Company has a revolving credit agreement with a group of banks for the borrowing of up to $75,000,000 to August 22, 1982, decreasing $15,000,000 annually to August 22, 1986 The most restrictive term of all borrowing agreements is under the revolving credit agreement, which limits the payment of cash dividends. Consolidated retained earnings not so restricted at June 30, 1981 amounted to approximately $115,750,000.

The Company is expected to maintain sufficient average bank balances to compensate those financial institutions that provide it with informal domestic lines of credit and the revolving credit agreement. Such balances are not legally restricted as to utilization or withdrawal and are generally met with normal operating balances

Long-Term Debt

Long-term debt due after one year consists of the following:

	June 30, 1981	June 30, 1980
	(In thousands)	
4½% convertible subordinated debentures due May 15, 1997	$100,000	$100,000
8⅛% Notes due February 15, 1985	90,000	90,000
Mortgage notes payable in various installments	2,715	2,844
Other	6,934	8,462
	$199,649	$201,306

The 4½% subordinated debentures are convertible into common stock at approximately $69 50 per share (1,438,800 shares) and are subject to redemption through annual sinking fund payments beginning in 1983 of not less than 6% nor more than 12% of the principal amount of debentures outstanding in 1982.

The 8⅛% Notes may not be redeemed before February 15, 1983. On or after that date, the Notes may be redeemed at the option of the Company in whole or in part at their principal amount, plus accrued interest.

At June 30, 1981, mortgage notes payable were collateralized principally by property, plant and equipment with a net carrying amount of approximately $5,126,000

Aggregate maturities of long-term debt in years 1982 through 1986 are: $4,305,000, $9,134,000, $7,655,000, $96,400,000 and $6,297,000.

Capital Stock

Changes in shares of capital stock during fiscal 1981, 1980 and 1979 are summarized below.

	Common	Preferred Series A convertible non-dividend	Preferred Series B convertible non-dividend
Shares authorized	30,000,000	5,000,000	
Stated value per share	$.50	$10	
Balance at July 1, 1978	21,228,588	169,717	26,797
Exercise of stock options	20,018		
Conversions of preferred stock	117	(57)	(393)
Redemptions		(18,000)	(969)
Balance at June 30, 1979	21,248,723	151,660	25,435
Exercise of stock options	51,934		
Conversions of preferred stock	49	(131)	(169)
Redemptions		(9,968)	(927)
Cancellation of treasury shares	(7,650)		
Awards of restricted stock	53,044		
Balance at June 30, 1980	21,346,100	141,561	24,339
Exercise of stock options	126,286		
Conversions of preferred stock	56	(82)	(169)
Redemptions		(7,562)	(2,147)
Awards of restricted stock	46,986		
Balance at June 30, 1981	21,519,428	133,917	22,023

Each Series A preferred share is convertible into .10 share of common stock and is also redeemable in whole or in part at the option of the holder Redemptions amounted to $60,000 in 1981, $71,000 in 1980 and $77,000 in 1979. Partial redemptions (aggregating $473,000 at June 30, 1981) do not reduce the number of shares outstanding. Series B preferred stock is convertible into .2974 share of common stock and is also redeemable The Company has the option to redeem both classes in whole or in part for $10 per share, less any amounts previously paid in partial redemption.

Authorized capital stock also includes 500,000 shares of 5% preferred stock, par value $100 per share, and 200,500 shares of 5% convertible preferred stock, par value $100 per share, none of which were outstanding during 1981, 1980 and 1979.

Shares of common stock were reserved as follows:

	June 30, 1981	1980	1979
Conversion of outstanding			
4½% convertible subordinated debentures	1,438,800	1,438,800	1,438,800
Series A convertible preferred stock	8,368	8,982	9,709
Series B convertible preferred stock	6,550	7,238	7,564
Stock options and restricted stock	2,029,643	2,202,915	2,308,143
	3,483,361	3,657,935	3,764,216

Stock Option and Long-Term Growth Incentive Plans

The 1971 Stock Option Plan provides for the granting of qualified and non-qualified options for the purchase of 500,000 shares of common stock. The 1974 Stock Option Plan, as amended, provided for the granting of qualified and non-qualified options for the purchase of 1,900,000 shares of common stock. The terms of the qualified and non-qualified options may not exceed five and ten years, respectively, and the option prices shall not be less than the fair market value of the common stock on the date of grant. At June 30, 1981, approximately 70 employees were eligible to continue participation in the Plans, and 280 employees held options to purchase shares of common stock. Options generally are exercisable one-third each year, cumulatively, beginning two years from date of grant. Options outstanding at June 30, 1981 are exercisable at various dates from September, 1984 to August, 1989 at an average purchase price of $27.55. There have been no charges to operations in connection with options granted to date.

Changes in options outstanding were:

	Shares	Option price per share
Outstanding at July 1, 1978	1,375,028	$23.69 to $48.56
Exercised	(20,018)	23.81 to 25.38
Cancelled	(48,188)	
Outstanding at June 30, 1979	1,306,822	23.69 to 48.56
Granted	5,000	29.00
Exercised	(51,934)	23.69 to 26.44
Cancelled	(38,050)	
Outstanding at June 30, 1980	1,221,838	23.69 to 48.56
Exercised	(126,286)	23.69 to 26.44
Cancelled or expired	(173,417)	
Outstanding at June 30, 1981	922,135	23.69 to 48.56

Options exercisable and available for future grant were:

	June 30, 1981	1980	1979
Exercisable	806,629	959,731	809,119
Available for future grant	1,107,508	981,077	1,001,321

The 1974 Plan was further amended to eliminate additional issuance of qualified options, and to authorize the granting of Restricted Stock and Performance Units, as well as the previously authorized stock options and stock appreciation rights, without increasing the maximum number of shares issuable under the Plan. At that time, the 1974 Plan was redesignated the Long-Term Growth Incentive Plan.

With certain exceptions, Restricted Stock awards are subject to specified periods of continuous employment (presently three years). The market value of shares at dates of award is deferred and amortized over the restriction period. Amortization expense charged to operations was $1,223,000 in 1981 and $551,000 in 1980. At June 30, 1981 and 1980, the unamortized deferred charge of $1,512,000 and $1,002,000, respectively, was included in other assets.

At the time of contingent cash awards, in the form of Performance Units, an award period is established during which certain goals must be met to enable the participants to receive full or partial payment. The value of a Unit will equal the fair market value of a share of common stock at the expiration of the award period. The value of Performance Units awarded is charged to operations over the award period. Compensation expense of $770,000 and $399,000 was charged to operations in 1981 and 1980, respectively.

Changes in outstanding Restricted Stock and Performance Units during fiscal 1981 and 1980 were:

	Restricted Stock	Performance Units
Outstanding at July 1, 1979	—	—
Granted	53,396	39,396
Cancelled	(352)	(352)
Outstanding at June 30, 1980	53,044	39,044
Granted	50,051	35,652
Cancelled	(3,065)	(3,065)
Outstanding at June 30, 1981	100,030	71,631

Pending Legal Proceedings

As more fully described in the Company's 1980 Annual Report to Shareholders, the Federal Trade Commission issued a complaint in 1972 which alleged a violation of the Clayton Act due to the Company's acquisition of 82% of United Vintners, Inc. This complaint was dismissed by the Federal Trade Commission during fiscal 1981 and is not subject to appeal.

Heublein and its subsidiaries are defendants in various litigation matters in which aggregate alleged damages are substantial. Based upon the advice of counsel, management believes Heublein and its subsidiaries have adequate defenses and that no material liability will result from such litigation

Business Segments

The Company operates worldwide principally in four business segments: production and marketing of distilled spirits and prepared cocktails (Spirits), production and/or marketing of wines and brandies (Wines), production and sale of specialty food products (Grocery) and operating and franchising principally Kentucky Fried Chicken restaurants (Restaurants) The business segment information for each of the three years ended June 30 is presented below.

	1981	1980	1979
		(In thousands)	
Revenues:			
Spirits	$ 876,546	$ 883,419	$ 819,563
Wines	378,497	386,938	368,972
Grocery	153,552	131,511	114,193
Restaurants	641,526	520,011	466,346
Consolidated	$2,050,121	$1,921,879	$1,769,074
Operating profit			
Spirits	$ 107,078	$ 93,341	$ 85,570
Wines	26,551	32,655	31,451
Grocery	21,545	17,904	17,989
Restaurants	69,126	51,302	34,966
Consolidated	224,300	195,202	169,976
Interest expense	28,581	25,361	23,106
Corporate and miscellaneous — net	27,378	23,783	15,851
Income before income taxes	$ 168,341	$ 146,058	$ 131,019
Identifiable assets:			
Spirits	$ 318,695	$ 320,379	$ 300,703
Wines	318,137	308,445	282,559
Grocery	61,601	63,219	66,696
Restaurants	316,519	276,682	244,330
Corporate	105,987	78,294	82,545
Consolidated	$1,120,939	$1,047,019	$ 976,833
Capital expenditures.			
Spirits	$ 4,386	$ 5,825	$ 6,980
Wines	7,148	14,885	20,414
Grocery	3,514	3,087	5,456
Restaurants	48,686	49,721	38,987
Corporate	250	336	1,059
Consolidated	$ 63,984	$ 73,854	$ 72,896
Depreciation and amortization.			
Spirits	$ 6,422	$ 6,393	$ 5,648
Wines	8,429	8,910	6,784
Grocery	3,143	3,644	3,243
Restaurants	23,546	19,616	16,766
Corporate	1,182	1,243	1,396
Consolidated	$ 42,722	$ 39,806	$ 33,837

Geographic area information is presented below

	1981	1980	1979
		(In thousands)	
Revenues			
United States	$1,602,543	$1,550,931	$1,428,183
Brazil	148,171	136,447	138,048
Remaining foreign geographic areas	299,407	234,501	202,843
Consolidated	$2,050,121	$1,921,879	$1,769,074
Operating profit			
United States	$ 168,081	$ 157,880	$ 139,938
Brazil	20,494	12,733	9,948
Remaining foreign geographic areas	35,725	24,589	20,090
Consolidated	$ 224,300	$ 195,202	$ 169,976
Identifiable assets:			
United States			
Operating assets	$ 752,504	$ 739,678	$ 682,772
Corporate	105,987	78,294	82,545
Brazil	119,388	95,529	97,181
Remaining foreign geographic areas	143,060	133,518	114,335
Consolidated	$1,120,939	$1,047,019	$ 976,833

Intersegment, intergeographical and export transactions are not significant.

Operating profit of each segment is total revenue less operating expenses. Operating profit excludes interest expense, income taxes and "Corporate and miscellaneous — net", which consists of interest income, equity in earnings of unconsolidated affiliates, general corporate expenses, minority interest in earnings of foreign subsidiaries and miscellaneous general expenses (see Management's Discussion and Analysis of Financial Condition and Results of Operations).

Corporate identifiable assets are principally cash and temporary investments.

Foreign exchange gains, principally in Brazil, for fiscal 1981, 1980 and 1979 were $5,447,000, $4,803,000 and $1,205,000, respectively. These exchange gains in Brazil are more than offset by lower reported profits when translated into U S dollars.

Operating profit of the Spirits, Wines and Grocery segments would have been higher in 1981 by $6,460,000, $658,000 and $1,860,000 and in 1980 by $5,229,000, $727,000 and $1,825,000, respectively, if the specific lot and FIFO inventory methods were used rather than the LIFO method (see Inventories note).

Pension and Deferred Compensation Plans

Pension expense, determined principally under the entry age normal actuarial cost method, amounted to $10,115,000 in 1981, $10,308,000 in 1980 and $9,137,000 in 1979

As of July 1, 1980, the actuarial present values of domestic vested and non-vested accumulated plan benefits were $32,098,000 and $8,435,000, respectively, and the net assets available for benefits were $53,712,000. The assumed rate of return used in determining the actuarial present values was 7%. The actuarial information and net assets available for benefits excludes the effects of the Company's foreign pension plans and the domestic multi-employer pension plans, whose present values are not separately determinable.

The Company's contribution under its Deferred Compensation Plan for salaried employees was the lesser of 8% of net income, as defined, or 8% of participants' salaries. Contributions amounted to $5,750,000 in 1981, $5,248,000 in 1980 and $4,651,000 in 1979.

Effective July 1, 1981, the Company amended the Deferred Compensation Plan to become a Savings and Investment Plan The Company will match employee contributions to a maximum of 6% of participant's compensation, as defined in the Plan. Of the approximately 4,000 employees eligible to participate in the Savings and Investment Plan, over 3,200 were participating at July 1, 1981.

Supplementary Income Statement Information

	1981	1980	1979
		(In thousands)	
Federal, state and foreign excise taxes	$459,317	$492,329	$466,211
Advertising, merchandising and sales promotion	$187,317	$168,913	$154,977
Maintenance and repairs	$ 23,971	$ 26,196	$ 23,426

Selected Quarterly Financial Data (Unaudited)

The following is a summary of selected unaudited quarterly financial data for the years ended June 30, 1981, 1980 and 1979 (in thousands except per share data):

	First quarter	Second quarter	Third quarter	Fourth quarter
1981				
Net sales	$458,010	$550,791	$468,361	$507,234
Franchise and license fees	17,389	16,087	15,118	17,131
Total revenues	$475,399	$566,878	$483,479	$524,365
Cost of sales	$318,202	$385,284	$324,610	$353,510
Net income	$ 23,080	$ 26,492	$ 17,890	$ 20,917
Earnings per share				
Primary	$1.07	$1 23	$ 83	$ 96
Fully diluted	$1 03	$1 18	$ 80	$ 93
1980				
Net sales	$438,554	$521,716	$432,040	$473,164
Franchise and license fees	15,573	13,466	12,513	14,853
Total revenues	$454,127	$535,182	$444,553	$488,017
Cost of sales	$311,280	$372,803	$307,736	$333,474
Net income	$ 20,184	$ 23,315	$ 15,624	$ 18,288
Earnings per share				
Primary	$ 95	$1 09	$ 73	$ 85
Fully diluted	$ .91	$1 04	$ .71	$ 82
1979				
Net sales	$414,605	$482,552	$396,217	$425,848
Franchise and license fees	14,039	11,932	10,578	13,303
Total revenues	$428,644	$494,484	$406,795	$439,151
Cost of sales	$297,647	$344,004	$282,162	$298,880
Net income	$ 17,627	$ 20,698	$ 13,950	$ 15,855
Earnings per share				
Primary	$ .83	$ .97	$ .65	$ .74
Fully diluted	$ .80	$ 93	$ .64	$ .72

Leases

The Company leases land, buildings and equipment. Many of these leases contain renewal options and some include escalation clauses All noncancellable leases with an initial term greater than one year have been categorized as capital or operating leases in conformity with Financial Accounting Standard No. 13, "Accounting for Leases"

Future minimum lease payments under noncancellable leases as of June 30, 1981 are summarized below:

	Capital leases	Operating leases
	(In thousands)	
Fiscal year ending June 30,		
1982	$ 5,545	$10,067
1983	5,288	7,958
1984	4,444	6,387
1985	3,884	4,974
1986	3,636	4,147
Thereafter	27,862	19,203
Total minimum lease payments	50,659	$52,736
Less amount representing interest	23,781	
Total obligations under capital leases	$26,878	

Rental expense under operating leases, net of minor sublease income, was $19,139,000 in 1981, $14,878,000 in 1980 and $14,732,000 in 1979 including contingent rental expense of $1,790,000, $1,372,000 and $1,072,000, respectively.

Supplementary Information on the Effects of Changing Prices (Unaudited)

As required by Financial Accounting Standard No. 33, "Financial Reporting and Changing Prices", the Company is presenting supplementary information designed to represent the effect of inflation on its operations.

Certain amounts appearing in the primary financial statements (inventories, property, plant and equipment, cost of sales and depreciation and amortization expenses) have been restated to two bases: "historical cost/constant dollars" and "current costs" The constant dollars restatement, through the use of the Consumer Price Index for all Urban Consumers, adjusts transactions recorded in actual dollars at different times to dollars having the same general purchasing power. The restatement to current costs is intended to reflect changes in specific prices. The use of various indices measuring price changes for specific types of assets was the principal technique used in estimating current costs These costs are meant to indicate the amount needed to replace existing inventories and production facilities at current prices.

Depreciation and amortization expenses are adjusted under both bases by restating the historical cost of property, plant and equipment to constant dollars and current costs for 1981. These restated costs become the base from which depreciation and amortization are calculated utilizing the same methods and asset lives used in historical cost statements Cost of sales is adjusted under both methods by restating the historical cost of inventories at the beginning and end of the year. No adjustment has been made for that portion of the Company's inventories valued by the LIFO method, since these amounts already approximate average fiscal 1981 dollars.

In accordance with Standard No. 33, no adjustments to income tax expense reported in the primary financial statements have been made in determining net income in the restated income statements. This provision is consistent with present tax laws which do not allow deductions for inflation adjusted costs. As a result, the consolidated effective income tax rate rises from 47.5% on the historical cost basis to 61.9% on the constant dollars basis and to 64.2% on the current costs basis.

Net monetary liabilities were held during a period in which the purchasing power of the dollar declined. As a result, the Company experienced a gain, since those monetary liabilities will be paid with dollars having decreased purchasing power. It should be noted that this purchasing power gain on net monetary liabilities does not represent receipt of cash and should not be considered as providing funds for subsequent reinvestment in the Company.

Both general and specific inflation adjustments involve estimates, assumptions and subjective judgments which should be viewed only as an attempt to approximate the effects of inflation. Clearly, these amounts are experimental in nature and may not represent the actual impact of inflation on the Company.

Consolidated Statement of Income
Adjusted for General Inflation and Specific Prices
Years ended June 30, 1981 and 1980
(In thousands except per share data)

	1981			1980*
	As reported in financial statements	Adjusted for general inflation (constant dollars)	Adjusted for specific prices (current costs)	Adjusted for specific prices (current costs)
Revenues	$2,050,121	$2,050,121	$2,050,121	$2,144,817
Cost of sales	1,381,606	1,411,337	1,418,348	1,514,299
Selling, advertising, administrative and general expenses	444,215	453,745	451,304	456,757
Other deductions	55,959	55,959	55,959	54,845
Income before income taxes	168,341	129,080	124,510	118,916
Income taxes	79,962	79,962	79,962	76,611
Net income	$ 88,379	49,118	44,548	42,305
Gain on net monetary items		21,632	21,632	34,634
Net income plus gain on net monetary items		70,750	66,180	76,939
Increase in specific prices**			83,943	114,271
Less effect of increase in general price level			81,326	119,734
Amount of increase in specific prices over (under) increase in the general price level			2,617	(5,463)
Net change in shareholders' equity from above	$ 88,379	$ 70,750	$ 68,797	$ 71,476
Per common share:				
Net income	$ 4 09	$ 2 27	$ 2 06	$ 1 98
Net income plus gain on net monetary items		$ 3 27	$ 3 06	$ 3 59
Net assets at year-end	$ 551,731	$ 772,682	$ 781,509	$ 771,087

*Amounts shown are stated in average fiscal 1981 dollars

**At June 30, 1981 and 1980 the current costs of inventory were $361,938,000 and $377,720,000 and the current costs of property, plant and equipment, net of accumulated depreciation, were $550,569,000 and $581,269,000, respectively

The adjustment to depreciation and amortization in 1981 increased cost of sales by $5,176,000 and $3,862,000 for constant dollars and current costs, respectively. Selling, advertising, administrative and general expenses were increased by $9,530,000 for constant dollars and by $7,089,000 for current costs, for a total depreciation and amortization effect of $14,706,000 and $10,951,000 under each basis. In 1980, the adjustment to current costs depreciation and amortization increased cost of sales by $4,793,000 and selling, advertising, administrative and general expenses by $8,900,000, for a total depreciation and amortization effect of $13,693,000

Heublein

Five Year Comparison of Selected Financial Data Adjusted for Effects of Changing Prices*

(Dollars in thousands except per share data)	Year ended June 30,				
	1981	1980	1979	1978	1977
Revenues	$2,050,121	$2,144,817	$2,236,110	$2,240,615	$2,289,131
Historical cost information adjusted for general inflation (constant dollars)					
Net income	49,118	51,958			
Net income per common share	2 27	2 43			
Net assets at year-end	772,682	753,841			
Historical cost information adjusted for specific prices (current costs)					
Net income	44,548	42,305			
Net income per common share	2 06	1 98			
Amount of increase in specific prices over (under) increase in the general price level	2,617	(5,463)			
Net assets at year-end	781,509	771,087			
Other information					
Gain from decline in purchasing power of net amounts owed	21,632	34,634			
Dividends declared per common share	1 78	1.81	1 88	1 91	1 90
Market price per common share at year-end	30 95	33 83	33 02	37.34	36 53
Average consumer price index	259 4	232.5	205 2	187 6	175 8

*Amounts shown are stated in average fiscal 1981 dollars

Report of Certified Public Accountants

ARTHUR YOUNG

ARTHUR YOUNG & COMPANY
277 PARK AVENUE
NEW YORK NEW YORK 10172

The Board of Directors and Shareholders
Heublein, Inc.

We have examined the accompanying consolidated balance sheet of Heublein, Inc. at June 30, 1981 and 1980, and the related consolidated statements of income, additional paid-in capital, retained earnings and changes in financial position for each of the three years in the period ended June 30, 1981 Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances

In our opinion, the statements mentioned above present fairly the consolidated financial position of Heublein, Inc at June 30, 1981 and 1980, and the consolidated results of operations and changes in financial position for each of the three years in the period ended June 30, 1981, in conformity with generally accepted accounting principles applied on a consistent basis during the period except for the change, with which we concur, to the LIFO method of accounting for certain inventories in the year ended June 30, 1980 as described in the Inventories note to the consolidated financial statements.

Arthur Young & Company

July 20, 1981

Liquidity and Capital Resources

Funds provided from operations of $130,906,000, $115,494,000 and $97,569,000 in 1981, 1980 and 1979, respectively, were the primary source of liquidity and capital funds In addition, the Company has traditionally used short-term debt to finance seasonal and other working capital requirements

At June 30, 1981, worldwide unsecured lines of credit totaling $91,763,000 were unused and available Additional credit of $75,000,000 was also available through the Company's revolving credit agreement Additional information on the above items is contained in the Company's "Temporary Investments and Short-Term Borrowings" note

Capital expenditures of $63,984,000 in fiscal 1981 declined from the 1980 level of $73,854,000 mainly due to the completion of several major projects at the Wines Group In fiscal 1982, the Company expects to spend in excess of $90,000,000 for capital expenditures, primarily for new KFC stores worldwide The Company anticipates these activities will be financed from internally generated funds

Changing Prices and the Effects of Inflation

For an explanation of the continuing effects of inflationary costs and changes in the purchasing power of the dollar, please refer to the "Supplementary Information on the Effects of Changing Prices" note discussed on pages 41 through 43

Results of Operations

The following discussion is presented to explain certain comparative changes shown in the Consolidated Statement of Income The Company's accounting policies, consolidated financial statements, notes to consolidated financial statements and shareholders' and operations letters should be read in conjunction with this discussion since they are all essential in evaluating the Company's results of operations

Fiscal year increase in the components of earnings	Increase 1981 compared to 1980 (In thousands)		Increase 1980 compared to 1979 (In thousands)	
Revenues	$128,242	6 7%	$152,805	8.6%
Cost of sales	56,313	4 2	102,600	8 4
Selling, advertising, administrative and general expenses	42,831	10 7	24,979	6 6
Interest expense	3,220	12 7	2,255	9 8
Corporate and miscellaneous — net	3,595	15 1	7,932	50 0
Income taxes	11,315	16 5	5,758	9 2

Revenues

Worldwide beverage sales declined 1% in 1981 after increasing 7% in 1980 The 1981 decline was mainly a result of the industry-wide slowdown in the domestic alcoholic beverage industry, and widespread inventory reductions by wholesalers and retailers in response to the high cost of short-term borrowings. Partially offsetting 1981's domestic beverage decline was a 9% increase in international beverage sales, attributable primarily to Brazil The 1980 sales increase in worldwide beverage was mainly due to good performances by both the domestic spirits and wines operations

Worldwide food sales increased 22% and 12% in 1981 and 1980, respectively. Both years' increases were due to gains in most major grocery products and higher per store averages at KFC both domestically and overseas in Australia, Mexico, South Africa and the United Kingdom

Management estimates that Company-wide price increases amounted to 7% and 3% in 1981 and 1980, respectively.

Cost of Sales

Increases in both years relate mainly to increased sales volumes The 1981 increase was partially offset by lower costs and excise taxes experienced in the domestic portion of worldwide beverage due to the volume shortfall Higher raw material prices, as well as greater manufacturing costs, were encountered throughout the Company Cost of sales in 1981 and 1980 increased $8,978,000 and $7,781,000, respectively, as a result of the change to the LIFO method of pricing certain inventories

Heublein

Selling, Advertising, Administrative and General Expenses

Increases for both years were due primarily to worldwide food's and domestic beverage's higher advertising, merchandising and sales promotion expenses and to increased retail KFC store operating costs, including additional worldwide stores. Lower selling expenses at the Wines Group, due to the closing of the wholesale operations last year, partially offset the 1981 increase. The 1980 variance was partially reduced by increased exchange gains.

Interest Expense

Higher interest rates in both years, coupled with increased borrowings in Brazil in 1981 and domestically in 1980, were the main contributors to the increases.

Corporate and Miscellaneous — Net

The 1981 increase was mainly due to costs associated with the settlement of the shareholders' derivative action litigation and to an 11% increase in corporate general and administrative expenses, primarily due to higher salaries and related benefits. Over $3,000,000 of the 1980 increase was due to lower interest income and equity in earnings of unconsolidated affiliates and higher miscellaneous general expenses. General corporate expenses increased more than 20% in 1980, including the impact of expenses related to the centralization of certain Company-wide functions.

Income Taxes

The consolidated effective income tax rates were 47.5% in 1981, 47.0% in 1980 and 48.0% in 1979. This year's increase is due principally to higher state and foreign taxes, while 1980's decline was due to a reduction in the statutory federal tax rate.

Responsibilities for Financial Statements

The financial statements included in this report were prepared by the Company in conformity with generally accepted accounting principles. These statements include certain amounts which are based upon informed estimates and judgments. Management is responsible for the integrity of the financial statements appearing in this annual report. Other financial information included in this report is consistent with these statements.

The Company maintains a system of internal controls which is designed to provide reasonable assurance that assets are safeguarded and that the financial records reflect the transactions of the Company. As a part of this process, the Company has an internal audit function which evaluates the adequacy and effectiveness of internal controls.

The Audit Committee of the Board of Directors is comprised of directors who are neither officers nor employees of the Company. The Committee meets periodically with management, internal auditors and independent certified public accountants to review the adequacy of internal control and financial reporting. The Director of Internal Audit and the independent certified public accountants have full and free access to meet with the Audit Committee with and without the presence of management.

Hicks B. Waldron

Hicks B. Waldron —
President and Chief Executive Officer

Gwain H. Gillespie

Gwain H. Gillespie —
Senior Vice President-Finance and Administration

Consolidated Selected Financial Data

(Dollars in thousands except per share data)	1981	1980**
Revenues	$2,050,121	$1,921,879
Costs and expenses		
Cost of sales	1,381,606	1,325,293
Selling, advertising, administrative and general expenses	444,215	401,384
	1,825,821	1,726,677
Operating profit	224,300	195,202
Income before income taxes	168,341	146,058
Income from continuing operations	88,379	77,411
NET INCOME	88,379	77,411
Earnings per common and common equivalent share:		
Continuing operations	$4.09	$3.62
NET EARNINGS	$4.09	$3.62
Earnings per common share assuming full dilution:		
Continuing operations	$3.93	$3.48
NET EARNINGS	$3.93	$3.48
STATISTICS:		
Dividends declared	$ 38,036	$ 34,566
Dividends declared per common share	1.78	1.625
Earnings retained in the business*	50,343	42,845
Taxes of all kinds*	563,835	588,007
Capital expenditures	63,984	73,854
Depreciation and amortization*	42,722	39,806
Net property, plant and equipment	388,594	372,043
Total assets	1,120,939	1,047,019
Long-term obligations and redeemable preferred stock	224,997	226,609
Working capital	286,551	264,999
Common and common equivalent shares (thousands)	21,626	21,404
Common shareholders	22,485	24,328
Worldwide employment	28,540	27,062
RATIOS:		
Current ratio	1.9 to 1	1.9 to 1
Return on shareholders' equity*	16.9%	16.3%
Income as a percent of revenues*	4.31%	4.03%

Restated where material (not restated for leases prior to 1975 since information was not available)
*Based on continuing operations
**After giving effect to a change to the LIFO method of valuing certain inventories (see Inventories note)

Heublein

1979	1978	1977	1976	1975	1974	1973	1972
1,769,074	$1,620,112	$1,550,902	$1,583,133	$1,414,415	$1,240,142	$ 966,139	$ 814,000
1,222,693	1,139,387	1,094,151	1,100,170	988,872	854,504	661,806	547,065
376,405	334,065	318,098	323,151	277,943	255,998	201,776	172,124
1,599,098	1,473,452	1,412,249	1,423,321	1,266,815	1,110,502	863,582	719,189
169,976	146,660	138,653	159,812	147,600	129,640	102,557	94,811
131,019	109,300	95,998	130,286	121,477	111,024	89,544	79,773
68,130	56,290	48,617	65,881	59,907	52,341	42,667	38,299
68,130	56,290	41,417	73,065	61,405	54,410	30,411	22,442
$3.19	$2.65	$2.27	$3.06	$2.82	$2.47	$2.04	$1.94
$3.19	$2.65	$1.93	$3.39	$2.89	$2.57	$1.45	$1.13
$3.09	$2.58	$2.22	$2.96	$2.71	$2.40	$1.99	$1.87
$3.09	$2.58	$1.91	$3.27	$2.78	$2.49	$1.45	$1.11
31,631	$ 29,269	$ 27,333	$ 24,838	$ 22,711	$ 20,497	$ 18,095	$ 15,921
1.49	1.38	1.29	1.175	1.075	.98	.91	.87
36,499	27,021	21,284	41,043	37,196	31,844	24,572	22,085
554,484	506,726	469,903	486,338	452,885	421,249	341,247	292,349
72,896	68,931	56,858	54,215	59,164	59,259	38,954	30,325
33,837	30,413	27,211	25,052	24,131	14,919	10,750	10,267
345,109	313,665	288,062	279,327	252,932	189,880	148,858	149,052
976,833	883,246	842,193	848,871	769,985	677,564	532,382	471,428
236,172	225,566	226,890	231,888	237,453	202,268	120,646	128,055
257,060	236,418	232,405	228,948	217,297	212,800	124,800	147,530
21,363	21,251	21,435	21,537	21,217	21,166	20,932	19,608
26,620	28,247	29,071	24,769	27,174	27,493	28,537	30,044
24,922	22,817	22,789	24,871	25,912	24,711	18,300	17,452
2.0 to 1	2.0 to 1	2.1 to 1	2.0 to 1	2.1 to 1	2.2 to 1	1.8 to 1	2.4 to 1
15.8%	14.1%	12.8%	19.0%	19.6%	19.3%	17.8%	18.8%
3.85%	3.47%	3.13%	4.16%	4.24%	4.22%	4.42%	4.71%

Directors

EDWARD B BATES
Chairman Connecticut Mutual
Life Insurance Company

CHRISTOPHER W. CARRIUOLO
Chairman Hartford Federal
Savings and Loan Association

LISLE C CARTER, JR.
President University of
The District of Columbia

JAMES F ENGLISH, JR.
President, Trinity College and
Chairman of the Trust Committee,
The Connecticut Bank and Trust Company

EDWARD H. HAMM
Vice President, The Northland Company
(A financial service company)

LEON W. HARMAN
President, Harman Management Corporation
(A franchisee for quick service restaurants)

RALPH A HART
Consultant and Retired Chairman
Heublein, Inc

CHARLES G. KLOCK
Retired President, General Electric
Credit Corporation

JOHN G. MARTIN
Consultant and Retired Chairman
Heublein Inc

ARTHUR A MILLIGAN
President Bank of A. Levy

WILLIAM H. MORTENSEN
Personal Investments

GERALDINE STUTZ
President
Henri Bendel

ROBERT L TRESCHER
The Sr Partner Law Firm of Montgomery
McCracken Walker & Rhoads

HICKS B WALDRON
President

STUART D WATSON
Chairman

Committees of the Board

EXECUTIVE COMMITTEE
STUART D WATSON*
EDWARD B BATES
JAMES F ENGLISH, JR
CHARLES G. KLOCK
JOHN G MARTIN
ROBERT L TRESCHER
HICKS B WALDRON

AUDIT COMMITTEE
ARTHUR A MILLIGAN*
LISLE C CARTER, JR
ROBERT L TRESCHER

COMPENSATION AND BENEFITS COMMITTEE
JOHN G MARTIN*
EDWARD B BATES
JAMES F ENGLISH, JR
CHARLES G. KLOCK
ROBERT L TRESCHER

FINANCE COMMITTEE
CHARLES G KLOCK*
EDWARD B BATES
JAMES F ENGLISH, JR
HICKS B WALDRON
STUART D WATSON

NOMINATING COMMITTEE
EDWARD B BATES*
JAMES F ENGLISH, JR
JOHN G MARTIN

SOCIAL RESPONSIBILITY COMMITTEE
LISLE C CARTER, JR *
CHRISTOPHER W CARRIUOLO
EDWARD H HAMM
LEON W HARMAN
GERALDINE STUTZ

*Chairman of Committee

Corporate Officers

STUART D WATSON
Chairman

HICKS B. WALDRON
President

GWAIN H. GILLESPIE
Senior Vice President — Finance
& Administration

MICHAEL A. MILES
Senior Vice President — Foods

JOHN A. POWERS
Senior Vice President —
Alcoholic Beverages

HUGH R. BEATH
Vice President — Group Executive
Grocery Products Group

JOHN F KELLER
Vice President — Group Executive
Wines Group

RICHARD P. MAYER
Vice President — Group Executive
Food Service & Franchising Group

BARRY M. ROWLES
Vice President — Group Executive
International Beverages Brazil Group

ROBERT R WEISS
Vice President — Group Executive
Spirits Group

GEORGE CASPAR
Vice President Secretary
and General Counsel

GENE R EHNEN
Vice President — Finance
and Controller

CHARLES J. HERBERT
Vice President — Spirits Sales Division

WILLIAM W. MAURITZ
Vice President — Human Resources

JOSEPH M. McGARRY
Vice President —
Communication and Public Affairs

JOHN J. MORAN
Vice President — Assistant to the Chairman

ROBERT W. PRATT, JR
Vice President — Planning and Research

THOMAS D. CHROSNIAK, JR.
Treasurer

Principal Offices

Corporate Headquarters
Farmington, Connecticut 06032 — (203) 677-4061

Beaulieu Vineyard
1960 St Helena Highway
Rutherford, California 94573 — (707) 963-3671

Food Service and Franchising Group Headquarters
1441 Gardiner Lane, Louisville, Kentucky 40232 —
(502) 459-8600

Kentucky Fried Chicken
Zantigo America's Mexican Restaurants
H Salt Seafood Restaurants

Grocery Products Group Headquarters
4 Farm Springs Drive
Farmington, Connecticut 06032 — (203) 677-7441

International Beverages/Brazil Group Headquarters
4 Farm Springs Drive
Farmington, Connecticut 06032 — (203) 677-7441

International Foods Group Headquarters
1441 Gardiner Lane, Louisville, Kentucky 40232

International Vintage Wines
330 New Park Avenue, Hartford, Connecticut 06101 —
(203) 233-7531

Spirits Group Headquarters
330 New Park Avenue, Hartford, Connecticut 06101 —
(203) 233 7531

Wines Group Headquarters
601 Fourth Street San Francisco, California 94107 — (415) 777-6500

United Vintners, Inc

Transfer Agents
The Bank of New York, 90 Washington Street, New York, New York 10015
Bank of America, N T & S A, 55 Hawthorne Street, San Francisco, California 94105

Registrars
The Bank of New York, 90 Washington Street, New York, New York 10015
Wells Fargo Bank, N A, P O Box 44011 San Francisco, California 94144

Trustees
4½% Convertible Subordinated Debentures
United States Trust Company of New York, 45 Wall Street, New York, New York 10005
8⅝% Notes
Morgan Guaranty Trust Company of New York,
30 West Broadway, New York, New York 10005

Annual Shareholders' Meeting

The annual meeting of shareholders of Heublein, Inc will be held at 10 00 a m Thursday, October 29, 1981 in the Assembly Hall of The Hartford Civic Center, One Civic Center Plaza, Hartford, Connecticut

Heublein's 1981 Annual Report on Form 10-K as filed with the Securities and Exchange Commission will be available upon request from the Corporate Secretary, Heublein, Inc, Farmington, Connecticut 06032.


SAINT JAMES
SAINT JAMES
BRISTOL
SMIRNOFF
VODKA
YUKON JACK
CANADIAN LIQUEUR
Arrow
MELON
A1
STEAK SAUCE
FOR SEASONING AND COOKING
"It's finger lickin' good".
HEUBLEIN
HEUBLEIN
HEUBLEIN
HEUBLEIN
Cuervo 1800
ORTEGA
ORTEGA
WHOLE GREEN CHILES
CLASSIC
Black & White
BUCHANAN'S
BLENDED SCOTCH
POPO
VODK
VODKA
1980
SERRALLES
DON Q
GOLD
RUM
BOGGS
Regina.
LANCERS

Heublein Brands of Foods and Beverages

Listed below are the principal brands of fine foods and beverages marketed by Heublein. When you have occasion to use products of this type, we invite you to order Heublein brands by name — you'll be getting the finest products of their kind.

Spirits:

Smirnoff Vodkas (80° & 100°) • Smirnoff Silver (90.4°) • Smirnoff de Czar Special Reserve Vodka (82.6°) • Black Velvet Canadian Whisky • Black & White Scotch • Arrow Cordials and Flavored Brandies • Heublein Cocktails • The Club Cocktails • José Cuervo Tequila • Cuervo 1800 • Don Q Rum • Irish Mist Liqueur • Milshire Gin • Popov Vodka • Relska Vodka • McMaster's Scotch and Canadian Whiskies • Matador Tequila • Malcolm Hereford's Cows • Yukon Jack Canadian Liqueur • Jeremiah Weed Bourbon Liqueur • Boggs Cranberry Liqueur • Vaklova Liqueur • Rhum St. James • Brandy Viejo Vergel

California Wines:

Beaulieu Vineyard Wines • Inglenook Vineyards Wines • Jacaré • Colony Table Wines, Dessert Wines and Aperitifs • Petri Wines • Annie Green Springs Refreshment Wines • T.J. Swann Refreshment Wines • H.M.S Frost • Esprit • G & D Wines and Vermouth • Lejon Champagne, Vermouth and Brandy • Lejon Soft Wines • Jacques Bonet Champagne and Brandy

Imported Wines:

Lancers Vin Rosé, Vinho Branco and Rubeo • Harveys Bristol Cream • Bouchard Pere & Fils Burgundy • Egri Bikaver Hungarian Wine • Tokaji Aszu Hungarian Dessert Wine • Harveys Other Sherries and Ports • Vinya Rosé • Kiku Masamune Sake • Taru Sake • Azura Italian Wine • Bouchard Pere & Fils Valbon Table Wines (White and Red) • Chateau Olivier Bordeaux • Ladoucette Loire Wines • Oliver de France • Valbon • Duval Vermouth • Conde de Caralt Sparkling Wine • Latour Cognac

Convenience Foods:

Kentucky Fried Chicken and Fixin's • H. Salt Seafood • Zantigo Mexican-American Foods

Sauces and Specialty Foods:

A.1. Steak Sauce • Grey Poupon Mustard • Ortega Tacos, Chiles and Sauces • Snap-E-Tom Tomato and Chile Cocktail • Regina Wine Vinegars and Cooking Wines • Escoffier Sauces • Steak Supreme Steak Sauce • Hart's Dinner Rolls, Muffins and Buttermilk Biscuits

Heublein

HEUBLEIN INC. FARMINGTON CONNECTICUT 06032